No. 488

In the Supreme Court of the United States

OCTOBER TERM, 1942

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

CHICAGO STOCK YARDS COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT

BRIEF FOR THE PETITIONER

INDEX

	Page
Opinions below	1
Jurisdiction	1
Question presented	2
Statutes and regulations involved	2
Statement	2
Specification of errors to be urged	22
Summary of argument	22
Argument	26
I. The Board's findings as to the character of the taxpayer's activities are supported by substantial evidence	41
II. The Board's finding that the taxpayer accumulated its profits beyond the reasonable needs of its business is wholly valid	69
III. In any event, the Board's determination is valid	76
Conclusion	83
Appendix	87

CITATIONS

Cases:	
Almours Securities v. *Commissioner*, 91 F. 2d 427, affirming 35 B. T. A. 61, certiorari denied, 302 U. S. 765, rehearing denied, 303 U. S. 656	45
American Textile Woolen Co. v. *Commissioner*, 68 F. 2d 820, certiorari denied, 293 U. S. 558	16
Baker v. *Commissioner*, 115 F. 2d 987	16
Berm Co. v. *Leedy*, 113 F. 2d 807	68
Black Diamond S. S. Corp. v. *National Labor Rel. Board*, 94 F. 2d 875, certiorari denied, 304 U. S. 573	55
Bleeker v. *Commissioner*, 103 F. 2d 487, affirming 37 B. T. A. 581, certiorari denied, 308 U. S. 576, rehearing denied, 308 U. S. 635	45, 80
Elmhurst Cemetery Co. v. *Commissioner*, 300 U. S. 37	30
Emerald Oil Co. v. *Commissioner*, 72 F. 2d 484	16
Fayish, W. S. S. & Co. v. *Commissioner*, 38 B. T. A. 150, affirmed, 101 F. 2d 833	80
Ginsberg & Sons v. *Popkin*, 285 U. S. 204	31
Gray v. *Powell*, 314 U. S. 402	45
Griffiths v. *Commissioner*, 308 U. S. 355	36
Helvering v. *Kehoe*, 309 U. S. 277	30
Helvering v. *Lazarus & Co.*, 308 U. S. 252	30

Cases—Continued. Page

Helvering v. *Nat. Grocery Co.*, 304 U. S. 282, rehearing denied, 305 U. S. 669 ..... 29, 30, 31, 38, 40, 62, 64, 75, 76, 78, 80, 82
Helvering v. *Northwest Steel Mills*, 311 U. S. 46 28
Helvering v. *Rankin*, 295 U. S. 123 ..... 30, 83
Helvering v. *Talbott's Estate*, 116 F. 2d 160 31
Higgins v. *Smith*, 308 U. S. 473 36
Insurance & Title Guarantee Co. v. *Commissioner*, 36 F. 2d 842, certiorari denied, 281 U. S. 748 16
Keck-Inv. Co. v. *Commissioner*, 77 F. 2d 244, affirming 29 B. T. A. 143, certiorari denied, 296 U. S. 633 45
Labor Board v. *Nevada Copper Co.*, 316 U. S. 105 30
McDonald v. *Thompson*, 305 U. S. 263 31
Noteman v. *Welch*, 108 F. 2d 206 28
Olin Corp. v. *Commissioner*, 128 F. 2d 185 64
Olson v. *Commissioner*, 67 F. 2d 726, certiorari denied, 292 U. S. 637 16
Pepper v. *Litton*, 308 U. S. 295 59
Perry, J. M., & Co. v. *Commissioner*, 120 F. 2d 123 ..... 31, 35, 64
Public Bank, Ex parte, 278 U. S. 101 31
R. & J., Inc. v. *Commissioner*, 84 F. 2d 721, affirming 33 B. T. A. 857, certiorari denied, 299 U. S. 588 45
Saeager, A. D., Inc. v. *Commissioner*, 84 F. 2d 23, certiorari denied, 299 U. S. 577 64
Sheppard & Myers, Inc. v. *Commissioner*, 45 F. 2d 50, certiorari denied, 282 U. S. 902 16
Texas & N. O. R. Co. v. *Ry. Clerks*, 281 U. S. 548 61
Tyco Products Corp. v. *Commissioner*, 46 B. T. A. 346 60
United Block Co. v. *Helvering*, 123 F. 2d 764, certiorari denied, 315 U. S. 812 35
United Business Corp. v. *Commissioner*, 62 F. 2d 754, certiorari denied, 290 U. S. 635 ..... 29, 35, 38, 64
United States v. *R. C. Tway Coal Sales Co.*, 75 F. 2d 336 35
Welch v. *Helvering*, 290 U. S. 111 31
Wickwire v. *Reinecke*, 275 U. S. 101 31
Willergod Daily Corp. v. *Commissioner*, 125 F. 2d 998 64
Williams Inv. Co. v. *United States*, 3 F. Supp. 225 ..... 60, 74, 81
Wilmington Trust Co. v. *Commissioner*, 316 U. S. 164 ..... 23, 30, 68
Wilson Bros. & Co. v. *Commissioner*, 124 F. 2d 606 ..... 45, 61

Statutes:

Internal Revenue Code, Sec. 102 (U. S. C., Title 26, Sec. 102) 28
National Industrial Recovery Act, c. 90, 48 Stat. 195, Sec. 214 ..... 27, 88
Revenue Act of 1921, c. 136, 42 Stat. 227, Sec. 220 34
Revenue Act of 1924, c. 234, 43 Stat. 253, Sec. 220 34
Revenue Act of 1928, c. 852, 45 Stat. 791, Sec. 104 ..... 23, 25, 27, 30, 34, 38, 41, 44, 83, 87

Statutes—Continued. Page

Revenue Act of 1932, c. 209, 47 Stat. 169, Sec. 104 ..... 23, 25, 27, 30, 34, 38, 41, 44, 83, 87

Revenue Act of 1934, c. 277, 48 Stat. 680, Sec. 351 28

Revenue Act of 1936, c. 690, 49 Stat. 1648, Sec. 14 28

Revenue Act of 1938, c. 289, 52 Stat. 447, Sec. 102 28

Tariff Act of 1913, c. 16, 38 Stat. 114, 166, Sec. II A 27

Miscellaneous:

Cong. Record, Vol. 65, Part 7, pp. 7354–7355 34

H. Rep. No. 179, 68th Cong., 1st Sess., p. 22 (1939–1 Cum. Bull. (Part 2) 257) 34

Morgan, *Some Observations Concerning Presumptions*, 44 Harv. L. Rev. 906, 912–914, 931–932 (1931) 31

S. Rep. No. 398, 68th Cong., 1st Sess., p. 26 (1939–1 Cum. Bull. (Part 2) 284) 34

Treasury Regulations 74:

Art. 541 89

Art. 542 ..... 66, 89

Art. 543 91

Treasury Regulations 77:

Art. 541 92

Art. 542 92

Art. 543 92

In the Supreme Court of the United States

OCTOBER TERM, 1942

No. 488

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

CHICAGO STOCK YARDS COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT

BRIEF FOR THE PETITIONER

OPINIONS BELOW

The opinions in the United States Board of Tax Appeals (III R. 932–956) are reported at 41 B. T. A. 590. The opinion of the Circuit Court of Appeals (IV R. 1265–1297) is reported at 129 F. 2d 937.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered July 24, 1942 (IV R. 1298). Petition for a writ of certiorari was filed in behalf of the

Commissioner of Internal Revenue on October 23, 1942 and was granted by this Court on December 7, 1942. The jurisdiction of this Court rests upon Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the Circuit Court of Appeals improperly rejected findings of the United States Board of Tax Appeals (a) that during the taxable years in question the taxpayer was a mere holding or investment company, (b) that it permitted its gains and profits to accumulate beyond the reasonable needs of its business, and (c) that it was availed of for the purpose of preventing the imposition of surtaxes upon its shareholders, within the meaning of Section 104 of the Revenue Acts of 1928 and 1932.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set out in the Appendix, *infra*, pp. 87–92.

STATEMENT

The central question is whether the taxpayer corporation, Chicago Stock Yards Company, was "availed of" during the years 1930, 1932, and 1933 for the purpose of preventing the imposition of surtaxes upon its stockholders by permitting its gains and profits to accumulate instead of being

distributed. The Commissioner determined that the taxpayer had been availed of for that purpose, and accordingly proposed to assess the 50% tax imposed by Section 104 of the Revenue Acts of 1928 and 1932 (I R: 27–34). The Board of Tax Appeals affirmed the Commissioner's determination, and approved the imposition of additional taxes for the years involved aggregating in excess of $4,000,000, plus interest (III R. 957–961, 1237–1239). The Board made extensive findings of fact (III R. 902–932, 957, 1202) which may be summarized as follows:

Chicago Stock Yards Company, a Maine corporation, referred to as the taxpayer, is the top holding company of what is sometimes called the Chicago stockyards enterprise. In addition to owning all of the stock of an operating utility company, Produce Terminal Corporation, as well as of other subsidiaries, the taxpayer controls the Chicago Junction Railways & Union Stock Yards Company, referred to as the Jersey Company, an intermediate holding company. The Jersey Company, in turn, owns all of the capital stock of several other operating companies, in which the great bulk of the stockyards enterprise is concentrated. (III R. 902–912.) Mr. Frederick H. Prince owns or controls all of the stock of the taxpayer (III R. 907–908, 909–910), and during the taxable years 1930, 1932, and 1933, avoided payment of surtaxes in excess of $1,300,000, because of the taxpayer's failure

to distribute its earnings (III R. 930–931).[1] See also footnote 4, *infra*, p. 7.

The Jersey Company and its subsidiaries.—The Jersey Company is a New Jersey corporation organized in 1890 for a period of fifty years (III R. 902). It has outstanding 65,000 shares of preferred stock and 65,000 shares of common stock, a share of each class being entitled to one vote. It also had outstanding $14,000,000 face value of non-callable bonds which were to mature in 1940.[2] The Jersey Company owns all of the capital stock (1) of the Union Stock Yards & Transit Company of Chicago, referred to as the Transit Company; (2) of the Chicago Junction Railway Company, referred to as the Railway Company; (3) of the Chicago Junction Railroad Company, referred to as the Elevated Company; and (4) all the shares of beneficial interest in the Central Manufacturing

---

[1] In this connection, there is also a finding that the taxpayer's stockholders failed to report and pay taxes on their proportionate interests in the undistributed earnings pursuant to Section 104 (d) of the Revenue Acts of 1928 and 1932 (III R. 931); had that been done, the taxpayer corporation would not have been subject to the taxes here involved.

[2] Of these, $4,000,000 bore interest at 4% and $10,000,000 bore interest at 5%. The $10,000,000 5% bonds were issued in 1915 to retire an issue of like amount which matured in that year (III R. 903). As collateral security for these bonds, the Jersey Company pledged substantially all of the outstanding shares of the Transit Company and of the Railway Company, referred to above, and $2,500,000 face value bonds of another, unrelated company (III R. 911).

District, a real estate trust referred to as the District. (III R. 902, 903–905, 910.)

(1) The Transit Company, which was organized as an Illinois corporation in 1865, operates the Chicago stockyards. During the years 1911–1913 more than 98% of its capital stock was owned by the Jersey Company and since 1913 it has been wholly owned by that company. On January 1, 1930, the Transit Company had outstanding debenture notes in the amount of $500,000. These were retired in that year and it has since had no bond or note obligations outstanding. (III R. 902.)

(2) The Railway Company, an Illinois corporation organized in 1898, is the lessee at a rental of $600,000 a year of the "Inner Belt," a railroad line serving the stockyards, which is owned by the Transit Company. In 1922 the Transit Company and the Railway Company jointly sub-leased the "Inner Belt" to a subsidiary of the New York Central Railroad Company for 99 years at a rental, guaranteed by the New York Central, of $2,000,000 per annum after the first year, the sub-lessee to pay all maintenance charges and taxes. The Railway Company has no outstanding indebtedness. (III R. 903–904.)

(3) The Elevated Company, an Illinois corporation, owns an elevated passenger railroad serving the area in Chicago known as Packingtown. In 1903 the Elevated Company leased this property

to the South Side Elevated Railroad Company, which connects with lines running throughout Chicago. In 1905 the Elevated Company issued $2,327,000 first mortgage 4% bonds due March 1, 1945, which are guaranteed by the Jersey Company. The rental for the railroad line is the payment of taxes and interest on the Elevated Company bonds. (III R. 904–905.)

(4) The District, which is the real-estate trust referred to, was created in 1902 to hold and acquire vacant land for development into a manufacturing district in order to provide additional tonnage for the "Inner Belt." The District had outstanding bonds of $2,915,000 in 1930, $2,700,000 in 1931, $2,475,000 in 1932, and $2,250,000 in 1933. All of these bonds had been guaranteed by the Jersey Company. (III R. 905.)[2]

The Produce Terminal Corporation, referred to as the Produce Terminal, is an Illinois corporation which supplies electric light and power to the Chicago stockyards. In 1926 the Jersey Company distributed all of the capital stock of Produce Terminal to the taxpayer as a dividend and since that date it has been wholly owned by the taxpayer.

[2] In June 1931 the District became the owner of all the capital stock of the Central Storage Corporation and the Central Storage & Forwarding Corporation, the former of which was merged into the latter in December of that year (III R. 911). In addition, the Transit Company owns all the capital stock of the Stock Yards Harness & Saddlery Company (III R. 905). These subsidiaries have no outstanding obligations (III R. 913) and seem to be of minor importance.

Produce Terminal has no outstanding indebtedness. (III R. 905–906, 913.)

The taxpayer.—The taxpayer corporation was organized under the laws of Maine in 1911 for the purpose of acquiring an interest in the stock of the Jersey Company (III R. 902). From 1911 to June 1922 Prince was the owner of about four-fifths of the taxpayer's capital stock and Armour was the owner of the remaining one-fifth (III R. 907–908). In the latter year Prince acquired Armour's holdings and has since continued to own all of its capital stock (III R. 909–910).[4] Under the 1911 plan for the formation of the taxpayer corporation, the common stockholders of the Jersey Company were offered the alternative of the taxpayer's guaranty, by way of a stamp on their stock certifi-

[4] In June 1932, Prince transferred a substantial portion of this stock to F. H. Prince & Company, Inc., a corporation owned entirely by him, and then transferred the stock of the corporation to himself and his wife as trustees for the benefit of certain relatives and friends (III R. 910). The court below observed (IV R. 1269) that the 1932 change of stock ownership "is assumed by both parties to be immaterial to the present litigation." Prince, in the deed of trust, had reserved to himself the exclusive right to vote the shares of F. H. Prince & Company, Inc., and retained continuing control of the taxpayer (III R. 910, 945–946).

It may be noted that the surtaxes avoided by Prince, in excess of $1,300,000 (*supra*, p. 3), do not include the taxes which were also avoided by F. H. Prince & Company, Inc., and the trust with respect to the second half of 1932 and the entire year 1933 (III R. 948). According to the computation introduced at the hearing, the trust during these years avoided taxes aggregating $1,143,303.09. (II R. 853–854, Ex. YYYY.)

cates, of $9 annual dividends or the privilege of exchanging their shares at the rate of one share for $200 face value of fifty-year 5% collateral trust bonds of the taxpayer. Under this arrangement, the assenting stockholders, on their part, assigned to the taxpayer all their rights to dividends from the Jersey Company upon the guaranteed shares, taxpayer agreeing that all dividends on such shares should first be used to pay the 9% guaranteed dividends. The taxpayer also agreed to secure its 5% bonds by unstamped Jersey Company $100 common stock for each $200 face amount of bonds or by shares of Jersey Company $100 preferred stock for each $120 face amount of bonds. (III R. 906–907.)

By August 31, 1914, the taxpayer had acquired in exchange for its bonds 31,075 Jersey Company common shares, and 33,922 shares had been stamped with its guaranty. In 1919 the taxpayer acquired the three remaining shares. (III R. 908.) By December 31, 1929, the taxpayer had acquired 58,742 shares of the Jersey Company's common and 457 shares of its preferred (III R. 912). During the tax years here involved, 1930–1933, the taxpayer added to its holdings in the Jersey Company, owning, at the end of 1933, 60,336 shares of common and 2,362 shares of preferred.[*]

[*] Of these additions, taxpayer purchased 253 shares of common in 1930, 380 shares in 1932, and 357 shares in 1933; it purchased 190 shares of preferred in 1930, 302 shares in 1932, and 797 shares in 1933 (III R. 927–928). Despite its

Of the 60,336 shares of common held at the end of 1933, the taxpayer had acquired 31,310 shares in exchange for $6,262,000 par value of its 5% bonds, and the remaining 29,026 shares for $4,979,352.19 cash (III R. 927). The taxpayer's outstanding liability upon such bonds was $3,227,000 as of December 31, 1929 (III R. 913), and $2,620,000 as of December 31, 1933 (III R. 919–920). Maturing in 1961, these bonds are taxpayer's only fixed obligations (III R. 913, 919, 920).

The bypass agreement.—By an agreement dated October 1, 1914, the taxpayer guaranteed the payment of the expenses of the Jersey Company, including the interest, but not the principal, upon its $14,000,000 of bonds outstanding and any payments of interest, but not of principal, which might be required under Jersey's guarantee of the $2,327,000 bonds of the Elevated Company. The taxpayer also guaranteed 6% dividends on the Jersey Company preferred stock and 9% dividends on whatever common stock the taxpayer had not acquired. On its part, the Jersey Company assigned to the taxpayer its right to all dividends distributable by the Transit Company and the Railway Company, as well as its entire net income after taxes. However, it was agreed that the Jersey Company should direct the Transit Company and the Railway Company to pay certain

---

large amount of cash on hand and the fact that they were readily procurable below par, the taxpayer purchased none of the bonds of the Jersey Company or the Elevated Company (III R. 924–927, 931).

specified amounts of interest on the Jersey Company bonds and dividends on its preferred stock and such common stock as the taxpayer had not acquired, and that the Jersey Company, in turn, should use its income first to pay its own expenses and taxes in each instance; any surplus was then to be paid to the taxpayer on its request. (III R. 908.)[7] The taxpayer has never been called upon to make any payments pursuant to its guarantees (III R. 931).

Other companies.—In addition to the wholly owned Produce Terminal, previously referred to (*supra*, p. 6), the taxpayer owns all of the capital stock of Western Associates, Inc., a Delaware corporation, organized in January 1933, to enable the taxpayer to hold stock in the Live Stock National Bank of Chicago (III R. 912). Apart from these subsidiaries, the taxpayer has had extensive dealings with F. H. Prince & Company, a brokerage and banking company wholly owned by Prince, with seats on the New York, Boston, and Chicago Stock Exchanges (III R. 908–909). Finally, the Pau Corporation, wholly owned by F. H. Prince & Company, was organized under Illinois law in 1931

[7] A copy of the agreement of October 1, 1914, is in the record as Exhibit 8-46. The exhibits are not printed but are certified to this Court in their original form.

This is true notwithstanding the fact that when the South Side Elevated Railroad Company, the lessee of the Elevated Company's line (*supra*, p. 6), went into receivership in 1932, the Jersey Company, as guarantor, paid the rental, which was used to pay the interest on the Elevated Company's bonds (III R. 930).

to take over the easements covering properties served with light and power by Produce Terminal. With money loaned to it by the taxpayer, upon which no interest was charged, the Pau Corporation also purchased machinery which was installed in the plant of Produce Terminal. (III R. 911–912.)

The structure of the Chicago stockyards enterprise on December 31, 1929.—Summarizing the situation at the threshold of the taxable years involved, the Board found that the taxpayer, upon a paid-in cash capital of $1,000,000, had an earned surplus of $19,615,905.69 and a capital surplus of $6,450. It owned all of the capital stock of Produce Terminal, carried at a value of $1,032,431.95, and of Central Manufacturing District Company,* carried at a cost of $506,448; 58,742 Jersey Company common shares out of 65,000 outstanding, carried at a cost of $10,993,551.74; and 457 Jersey Company preferred shares out of 65,000 outstanding, carried at a cost of $45,821.50. Produce Terminal was a prosperous corporation. It had net earnings of $262,213.73 for 1929 and annual average earnings of $172,517.68 for the five-year period ended with 1929. It paid dividends to the taxpayer from 1928 to 1933, inclusive, at the rate of $200,000 per annum. Its excess of assets over liabilities at Decem-

* This Company was organized pursuant to a plan for the purchase by Prince of Armour's shares in the taxpayer; it is of no present importance and is to be distinguished from the Central Manufacturing District, the real estate trust referred to above (III R. 909–910).

ber 31, 1929, was $2,352,017.05, although carried on the taxpayer's books at a value of $1,032,431.95. (III R. 912–913.) The taxpayer had outstanding at December 31, 1929, 5% bonds in the amount of $3,227,000. Its excess of assets over all liabilities, including its capital stock on that date, was $19,622,355.69. (III R. 913.)

The Jersey Company owned all the shares of capital stock of the Transit Company, the Railway Company, the Elevated Company, and the entire beneficial interest in the District. It filed a consolidated return for 1929, which included the operations of these wholly owned subsidiaries (including the operations of the Harness & Saddlery Company, a subsidiary of the Transit Company) and showed a net income of $2,835,383.71 for the entire group. The group had outstanding bonds and debenture notes as follows (III R. 913):

Jersey Co. 5% bonds maturing 4 1 40	$10,000,000
Jersey Co. 4% bonds maturing 4 1 40	4,000,000
Elevated 4½ bonds maturing 3 1 45	2,327,000
District bonds maturing at various dates	3,809,000
Transit Co. debenture notes maturing 1930	600,000
Total	20,736,000
Net consolidated assets	$73,322,871.58
Net consolidated liabilities	33,191,175.08
Excess of assets	40,131,696.50

Against the total bonded indebtedness of $23,963,000 standing against the entire group of companies (i. e., the $3,227,000 indebtedness of the taxpayer plus the $20,736,000 indebtedness of the Jersey Company and its subsidiaries), were the following liquid assets (III R. 914):

Taxpayer:	
Cash	$6,689,304.26
Accounts receivable	252,447.08
Notes receivable (Prince)	3,404,400.00
District 6's 1930	27,000.00
District 5's	55,733.40
Transit Co. 5½'s	15,022.50
Other investments	1,467,338.35
Produce Terminal:	
Cash	499,575.93
Total	12,410,821.12
Jersey Co. and subsidiaries*	9,594,363.94
Total	21,705,185.06

*Includes impounded charges of $2,013,523.54 which were not released to the Transit Co. until 1932.

In addition to the above, the taxpayer and the Jersey Company and its subsidiaries owned fixed and other assets of a book value of approximately $40,000,000 (III R. 914).

The taxpayer's balance sheets.—The taxpayer's balance sheets for the years 1929 to 1933, inclusive, revised to reflect correct earned surplus, are set out in full in the Board's findings (III R. 918–919). A comparison of the balance sheets as of December 31, 1929, and December 31, 1933, shows that the taxpayer's earned surplus increased from $19,615,905.69 to $28,259,278.70, as of December 31, 1933, or by $8,643,373.01.* Of the earned surplus at the

*The Board pointed out that an item carried in the balance sheets as "Investment Account"—$7,000,000—had never had any asset value, but represented the capital stock issued for the 1911 plan (III R. 919–920). This item is offset by the capital stock, carried at $8,000,000, of which only $1,000,000 was issued for cash. In addition, the Board referred to other items which disclosed an actual earned surplus substantially in excess of that reported on the balance sheets (III R. 920).

end of 1933, $7,645,235.97 was in cash and represented an increase in cash over 1929 of $955,931.71, not taking into consideration certain subordinated bank deposits, hereafter referred to, in the amount of $1,800,000. (III R. 918–919.)

The taxpayer's income.—The taxpayer's net earnings and dividends paid for the years 1911–1933 are shown in the following tabulation (III R. 918):

Year	Net earnings	Dividends paid	Excess of net earnings
	$	$	$
1911–1929	24,375,905.69	4,760,000	19,615,905.69
1930	3,468,336.80	400,000	3,068,336.80
1931	2,338,232.14	400,000	1,938,232.14
1932	2,172,963.09	400,000	1,772,963.09
1933	2,243,840.98	400,000	1,843,840.98
Totals	34,619,278.70	6,360,000	28,259,278.70

As shown by this table, the taxpayer's net earnings for the four years, 1930–1933, were $10,243,373.01. Of these earnings, $1,600,000 was paid out in dividends and $8,643,373 is reflected in earned surplus. Of the latter sum, $8,069,074.36 represents an increase in assets, and $574,298.65 a reduction of liabilities. (III R. 919.)

Income and financial condition of the enterprise, 1930–1933.—The Board also found, in tabular form, the net earnings of the entire enterprise during the years 1930–1933, inclusive, as well as the separate earnings of the Jersey Company, its subsidiaries and Produce Terminal (III R. 921–924). As of December 31, 1930, and December 31, 1933, the

earned surpluses of these companies were as follows (III R. 922–924):

	1930	1933
Jersey Company	$8,062,693.22	$4,203,805.76
Transit Company	5,019,956.05	3,718,951.06
Railway Company	2,073,881.72	2,425,521.83
Elevated Company	*57,361.55	*134,635.97
District	5,126,553.50	5,699,978.65
Produce Terminal	1,039,253.66	1,182,516.98

* Deficit.

Use made by taxpayer of its funds, 1930–1933.— During these years the taxpayer, apart from disbursing dividends in the aggregate amount of $1,600,000, reduced its liabilities by $574,298.65 (*supra*, p. 14); added to its cash on hand $2,755,931.71, $1,800,000 of which was subordinated to the claims of other depositors in a stockyards bank;[10] loaned to the District $1,625,000 to enable it to pay off some of its bonds and improve its properties; increased its loans to Prince, which are hereinafter referred to, in the amount of $1,743,600; loaned $236,536.51 to the Pau Corporation (wholly owned by Prince), without interest; invested $1,500,000 in the shares of Western Associates, Inc. (*supra*, p. 10); spent $245,800.45 for 1,594 shares of common and $173,111.83 for 1,905 shares of preferred stock of the Jersey Company (*supra*, p. 8); spent $423,107.25 in the purchase of $609,000 par value of its 5% bonds, maturing in 1961; and various

[10] During this same period the Transit Company, Produce Terminal, and the District subordinated deposits of $2,200,000 in order to assist stockyards banks (III R. 915).

amounts in the purchase of other securities (III R. 927, 940). The taxpayer also invested $3,573,218.77 in securities of stockyards banks [11] which needed bolstering (III R. 915). With respect to the advances to the District and the Pau Corporation, the Board found that the necessity for these loans, if any existed, was not shown (III R. 942). With respect to the loans to Prince, the Board found that there was no satisfactory explanation as to why the taxpayer did not make dividend distributions to Prince of the funds which he needed (III R. 947). And concerning the taxpayer's general use of its funds, the Board also expressly found that taxpayer was free to use them in any manner it saw fit [12] (III R. 941–942).

Prince's indebtedness to the taxpayer.—At the end of each year from 1911 to 1933, inclusive,

---

[11] During these same years the Transit Company and Produce Terminal invested some $3,750,000 in such securities (III R. 914–915).

[12] While some of the statements contained in the above and succeeding paragraphs are taken from determinations of fact appearing in the body of the Board's opinion which are not separately denominated as "findings," it is settled that they are nonetheless findings and are to be treated as such. *Baker* v. *Commissioner*, 115 F. 2d 987 (C. C. A. 6th); *Shippaid & Myers, Inc.* v. *Commissioner*, 45 F. 2d 50 (C. C. A. 3d), certiorari denied, 282 U. S. 902; *Emerald Oil Co.* v. *Commissioner*, 72 F. 2d 681 (C. C. A. 10th); *American Textile Woolen Co.* v. *Commissioner*, 68 F. 2d 820 (C. C. A. 6th), certiorari denied, 293 U. S. 558; *Olson* v. *Commissioner*, 67 F. 2d 726 (C. C. A. 7th), certiorari denied, 292 U. S. 637; *Insurance & Title Guarantee Co.* v. *Commissioner*, 58 F. 2d 842 (C. C. A. 2d), certiorari denied, 281 U. S. 748.

Prince or his wholly owned brokerage house, F. H. Prince & Company,[13] was indebted to the taxpayer (III R. 915–916). At the end of 1911 the debt amounted to $300,000; it steadily increased up to 1921, reaching $760,000. The loans, both of cash and securities, by the taxpayer to Prince or F. H. Prince & Company at the end of each year from 1922 to 1933, inclusive, were as follows (III R. 916):

Year	Cash	Securities	
		Bonds Taxpayer and United States Treasury	Stock New Jersey Company Common Shares
1922	$760,000 00	$150,000	16,855
1923	785,000 00	160,500	16,855
1924	780,000 00	164,000	15,355
1925	760,000 00	172,000	15,365
1926	947,867 08	172,000	14,755
1927	1,080,000 00	150,000	13,000
1928	1,700,000 00	80,000	11,000
1929	3,104,400 00	170,000	6,000
1930	2,520,400 00	150,000	4,200
1931	2,519,400 00	241,000	3,400
1932	3,408,000 00	91,000	1,710
1933	4,848,000 00	45,000	1,800

Prince and the brokerage company paid interest on cash borrowed from the taxpayer at the rate of 4% per annum, but nothing for the securities bor-

[13] In connection with these loans the Board did not distinguish between Prince and F. H. Prince & Company (III R. 915, fn. 3). The latter was wholly owned by Prince, its business was reported in his individual tax return, and for purposes of the present case the two are "identical" (I R. 106–107). F. H. Prince & Company is to be distinguished from the *corporation* F. H. Prince & Company, Inc., referred to in footnote 4, *supra*, p. 7.

rowed. From 1912 to 1933 collateral was pledged with the taxpayer to secure the cash loans, consisting principally of the taxpayer's common stock. The fair market value of the collateral so pledged was $3,673,608 at the end of 1930, $5,541,695.20 at the end of 1932, and $8,664,199 at the end of 1933. (III R. 916–917.)

These loans were used by Prince for any purpose desired by him. In 1932 Prince borrowed $160,000 from the taxpayer for the purchase of a home at Newport, Rhode Island, and $450,000 in order to strengthen the financial statement of F. H. Prince & Company. In 1933 he borrowed an additional $440,000 for the same purpose and $1,000,000 to enable him to acquire stock in Armour & Company. The latter loan enabled Prince to become chairman of the board of directors of Armour & Company and thus to retain its business for the Chicago stockyards. (III R. 917, 926.)[14]

---

[14] The taxpayer's status as a vehicle for tax avoidance is further illuminated by the fact that during the years 1931–1933 F. H. Prince & Company "sold" various securities to it, most of them apparently unrelated to the stockyards enterprise, and thereby enabled Prince to establish losses in substantial amounts which he deducted from his taxable income for those years. Those deductions amounted to $196,124.68 in 1931, $221,629.08 in 1932, and $93,102.22 in 1933. (III R. 928, 929.) Moreover, in 1932 the taxpayer sold to F. H. Prince & Company, Inc., 3,050 shares of the Chicago Stock Yards National Bank and 240 shares of Central Manufacturing District Bank at a loss to the taxpayer of $221,202.03 (III R. 929).

The Board also refers to another use made of the taxpayer by Prince resulting in a reduction of his own tax

The taxpayer's principal activity.—The taxpayer's income during the years 1930–1933 consisted exclusively of interest, dividends, and profit upon sales of securities. Its tax returns for these years described its business as that of "acquiring and guaranteeing securities." It received no fees for the management and supervision of any of its subsidiaries. It had practically no office expenses; it paid no rent except vault rent; and its office was Prince's office at 1 Court Street, Boston. The taxpayer paid its treasurer a salary of $500 and "wages" of $2,000 a year. Apart from the $50,000 salary which it paid its president, Prince, the taxpayer paid no other salaries or wages. McDonough, its vice president [18a] and Prince's secretary, did not receive any salary from the taxpayer. (III R. 922, 937.) During the years 1930–1933, and prior to that period, the taxpayer's principal activity was the purchase and holding of securities, the collecting of dividends, and the lending of money to Prince (III R. 931).

---

liabilities. Over a period of several years F. H. Prince & Company had accumulated approximately 18,000 shares of Jersey Company common, upon which it was receiving an annual dividend of $9 per share. These shares belonged to F. H. Prince & Company, and hence to Prince individually, and were not purchased for the account of the taxpayer. In 1918 the shares were transferred to the taxpayer at cost. This transaction relieved Prince of the payment of surtaxes upon the dividends received from these shares. (III R. 927, 947.)

[18a] McDonough, in fact, did not become vice president of the taxpayer until after the taxable years here involved (*infra*, p. 55).

In addition to his salary from the taxpayer, Prince received the following annual salaries from the taxpayer's subsidiaries in the capacities indicated below (III R. 929):

President of the Jersey Co.	$17,500.00
Chairman of the board of directors of the Transit Co.	17,500.08
Chairman of the board of directors of the Railway Co.	12,499.92

The returns of the Transit Company and the Railway Company reported Prince as devoting 58% of his time to the former and 42% to the latter (III R. 938). Although Prince actively supervised the operations of the Jersey Company and its subsidiaries as well as the subsidiaries of the taxpayer, he was enabled to do so through his ownership of all of the taxpayer's stock. In directing the affairs of these companies (III R. 929–930) he was acting as a paid officer or employee of these companies and not of the taxpayer (III R. 938).

In addition to its numerous subsidiary findings, the Board made three critical ultimate findings (III R. 932):

> 44. During the years 1930, 1932, and 1933 the petitioner was a mere holding or investment company.
>
> 45. During the years 1930, 1932, and 1933 the petitioner permitted its gains and profits to accumulate beyond the reasonable needs of its business.
>
> 46. During the years 1930, 1932, and 1933 the petitioner was availed of for the purpose of preventing the imposition of the surtax upon its stockholders through the medium of permitting its gains or profits to accumulate instead of being divided or distributed.

These three separate findings form the basis of the Board's decision against the taxpayer on three independent grounds: (1) Since the taxpayer was a "mere holding or investment company," the presumption set forth in Section 104 (b) was operative and the evidence failed to rebut that presumption; (2) the accumulation of earnings beyond the taxpayer's reasonable needs similarly brought the same presumption into play and the evidence here likewise failed to rebut the presumption; and (3) in any event, even without the benefit of the statutory presumptions, the record establishes that the taxpayer was "availed of" within the meaning of Section 104 (a) for the condemned purpose (III R. 945).

Reversing the decision of the Board, the Circuit Court of Appeals rejected as without support in the evidence the Board's determination that the taxpayer was a "mere holding company" (IV R. 1285). Secondly, the court rejected the Board's finding that the taxpayer's earnings were permitted to accumulate beyond the reasonable needs of its business, on the ground that the Board had used an improper "legal yardstick" in measuring such needs (IV R. 1290). Thirdly, the court rejected the Board's final determination, which was reached without the aid of the presumptions, on the ground that it rested "chiefly" on the Board's findings under the first and second points (IV R. 1296).

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In overturning the determination of the Board of Tax Appeals that the taxpayer was a mere holding or investment company.

2. In overturning the Board's determination that the taxpayer had accumulated its gains and profits beyond the reasonable needs of its business.

3. In overturning the Board's determination that the taxpayer was availed of for the purpose of preventing the imposition of the surtax upon its stockholders through the medium of permitting its gains or profits to accumulate instead of being divided or distributed.

4. In failing to accord the full effect to the presumption established by Section 104 (b) of the Revenue Acts of 1928 and 1932.

5. In holding that the projected 1940 liquidation of the Jersey Company, coupled with the acquisition of sufficient Jersey Company common and preferred stock to be able to control the liquidation, was a reasonable need of the taxpayer's business.

6. In remanding the case upon a false issue.

7. In reversing the judgment of the Board.

SUMMARY OF ARGUMENT

I

The Board rejected the taxpayer's claim that it supervised and directed the entire stockyards enterprise and acted as "banker" for it. Appraising

the evidence, the Board found instead that the taxpayer had merely an investment interest in the enterprise, and that its funds, rather than being dedicated to the requirements of the Jersey Company and the operating companies, were commanded by Prince in the accumulation of a vast personal fortune. The Circuit Court of Appeals overturned the Board's findings as not "permissible", and found for itself that the taxpayer did supervise and direct the enterprise and did act as banker for it. This conclusion the court reached only by appraising the evidence for itself, picking and choosing from among bits of evidence which pointed in opposite directions, and by tearing from their context certain of the Board's subsidiary findings. This the court was not at liberty to do.

On the basis of its subsidiary findings, the Board made the ultimate finding that the taxpayer was "a mere holding or investment company" within the meaning of Section 104 (b). That finding of the Board was just as much a finding of fact as its determination in *Wilmington Trust Co.* v. *Commissioner*, 316 U. S. 164, that a certain transaction was not a "short sale." If the reviewing court had no authority to reject the finding in that case, there was similarly no authority to do so here. And since the Board found that the presumption which was called into play by that finding had not been overcome by the evidence adduced in behalf of the taxpayer, this was enough to dispose of the case.

II

In the alternative, the Board found that even if the taxpayer were not a mere holding or investment company, the Commissioner's determination was correct. For, the Board concluded that, even considering the taxpayer as a management company in the stockyards enterprise, the earnings had been accumulated beyond the reasonable needs of the taxpayer's business within the meaning of Section 104 (b). In support of that finding the Board noted, *inter alia*, that the taxpayer's accumulated profits as of December 31, 1929, amounted to some $20,000,000 and were more than ample to provide for the retirement of its outstanding bonds, aggregating $3,227,000 and maturing in 1961, and any contingent liability under its guaranty of certain payments connected with the Jersey Company. The Board concluded that the taxpayer's evidence failed to overcome the presumption brought into play by the foregoing finding that its earnings had been accumulated beyond the reasonable needs of its business.

In overturning this ultimate finding the court professed to base its ruling on the ground that the Board had used an erroneous "legal yardstick" in determining the taxpayer's business needs. The Jersey Company's charter was to expire in 1940, and the taxpayer asserted in substance that it intended to use the accumulated earnings to buy out the "minority" interests and "liquidate" the

Jersey Company in 1940. The Board had ruled that such a purpose was merely in furtherance of Prince's plans to obtain complete ownership of the stockyards enterprise, and did not represent reasonable business needs. In deciding otherwise, the court below really differed with the Board on a question of fact. It should not have remanded the case for further proceedings to determine whether the accumulations were necessary for the so-called liquidation of the Jersey Company. The issue left open on the remand is a false one, for the Board had already determined that the "liquidation" of the Jersey Company was not within the reasonable needs of the business.

III

Finally, the Board considered the evidence without the aid of the statutory presumptions discussed above in Points I and II, and, so appraising the evidence, made its third critical finding that the taxpayer had been "availed of" to avoid surtaxes on its shareholders within the meaning of Section 104 (a). The court below rather lightly put aside this finding, stating that it "was predicated chiefly" upon the two findings discussed above in Points I and II, which the court had already rejected.

But the court was seriously mistaken in thus treating this third ultimate finding, for the Board had explicitly stated that it was reached without

the benefit of the statutory presumptions brought into play by the other two findings, and had outlined the dominant considerations which led it to make this third ultimate finding, saying (III R. 945):

> Even without the benefit of the statutory presumptions, we think there is sufficient evidence in the record to show the existence of the condemned purpose. The bare recital of the undisputed facts relating to the organization of the petitioner, the balance sheets, the source of earnings, the nature of the investments, the large accumulations of cash and surplus, the loans of cash and securities to the petitioner's sole stockholder, and the continued reinvestment of its gains and profits in securities, present, in our opinion, a situation typical of situations which Congress intended to cover by section 104 of the Revenue Acts of 1928 and 1932.

Accordingly, unless the Board is to be disbelieved, it actually placed its decision upon this third independent alternative ground. The finding upon which that ground rested was amply supported by the record, and should not have been disturbed on appeal.

ARGUMENT

This case involves Section 104 of the Revenue Acts of 1928 and 1932. The sections are identical except as subdivision (a) of Section 104 of the 1932 Act was amended in a respect unimportant for

present purposes by Section 214 of the National Industrial Recovery Act (Appendix, *infra*, pp. 87–88). Subdivision (a) of Section 104 of both Acts lays a 50% tax upon the "net income" of any corporation which is—

> formed or availed of for the purpose of preventing the imposition of the surtax upon its shareholders through the medium of permitting its gains and profits to accumulate instead of being divided or distributed * * *.

Subdivision (b) provides that the fact that any corporation is a mere holding or investment company or that its gains or profits are permitted to accumulate beyond the reasonable needs of the business "shall be prima facie evidence of a purpose to escape the surtax." Subdivision (c) defines the "net income" upon which the tax is measured, and subdivision (d) provides that the tax shall not apply if all of the shareholders of the corporation include in their gross income their entire distributive shares of the net income of the corporation, whether distributed or not.

The tax imposed by these sections [15] is dependent upon the "purpose" of those in a position to control the corporation. In this respect, the tax imposed by Section 104 differs from the tax imposed upon the undistributed profits of personal holding

[15] Comparable provisions have been in every revenue act since the adoption of the Sixteenth Amendment. The first such provisions appeared in Section II A, Subdivision 2 of the Tariff Act of 1913, c. 16, 38 Stat. 114, 166.

companies by Section 351 of the Revenue Act of 1934, c. 277, 48 Stat. 680 (see *Noteman* v. *Welch*, 108 F. 2d 206 (C. C. A. 1st)), and the tax imposed upon the undistributed profits of corporations generally, other than personal holding companies, by Section 14 of the Revenue Act of 1936, c. 690, 49 Stat. 1648 (see *Helvering* v. *Northwest Steel Mills*, 311 U. S. 46). It should be observed, however, that in imposing the taxes upon undistributed profits without regard to purpose in the Revenue Acts of 1934 and 1936, Congress did not abandon the tax involved in the instant case. Instead, it continued and strengthened it. By Section 102 of the Revenue Act of 1938, c. 289, 52 Stat. 447, the fact that the earnings of a corporation are permitted to accumulate beyond the reasonable needs of the business is made—

> determinative of the purpose to avoid surtax upon shareholders unless the corporation by the clear preponderance of the evidence shall prove to the contrary.[18]

As amended in this and other respects, the tax here involved has been carried into the Internal Rev-

[18] It appears that the 1938 amendment would have had no effect on the instant case since here the Board of Tax Appeals determined that the taxpayer failed to rebut the presumption arising from its unreasonable accumulation of earnings even by a bare preponderance of the evidence; and if the presumption itself has been properly established, the question whether it has been overcome, as we point out, *infra*, p. 35, is a matter for the trier of fact which the reviewing court is powerless to disturb.

enue Code, Section 102 (U. S. C., Title 26, Sec. 102).

Since the tax depends upon purpose or motive, the application of Section 104 turns upon the state of mind of the person or persons in control of the corporation. This, of course, is not novel, for both at common law and under statutes liability not infrequently depends upon a person's mental state. *Helvering* v. *Nat. Grocery Co.*, 304 U. S. 282, 289–290, rehearing denied, 305 U. S. 669; *United Business Corp.* v. *Commissioner*, 62 F. 2d 754, 756 (C. C. A. 2d), certiorari denied, 290 U. S. 635. As in other fields of the law involving a subjective state, the trier of fact is not required to accept at face value the denials of the person whose purpose or motive is in issue, but may base its ultimate determination upon circumstantial evidence of rational probative force. *Helvering* v. *Nat. Grocery Co.*, 304 U. S. at p. 295. Thus, in cases such as this, it becomes highly relevant to investigate the scope and character of the corporation's business, to inquire whether profits have been accumulated in excess of the reasonable needs of the business, and to examine all pertinent transactions between the corporation and its stockholders.

Plainly, such questions as the scope and character of the taxpayer corporation's activities, its reasonable business needs, its dealings with its stockholders, and the ultimate determination

of the existence of the forbidden purpose are pure questions of fact for the Board or trial court to decide. If the findings of the trier of fact are supported by substantial evidence, and are untainted by errors of law, they are conclusive upon review. *Helvering* v. *Nat. Grocery Co.*, *supra*; *Wilmington Trust Co.* v *Commissioner*, 316 U. S. 164; *Helvering* v. *Kehoe*, 309 U. S. 277; *Helvering* v. *Lazarus & Co.*, 308 U. S. 252; *Elmhurst Cemetery Co.* v. *Commissioner*, 300 U. S. 37; *Helvering* v. *Rankin*, 295 U. S. 123. It is of no moment that there may be substantial evidence to support a finding contrary to that made by the Board or trial court. As this Court has recently said, referring to findings made by the National Labor Relations Board, "The possibility of drawing either of two inconsistent inferences from the evidence did not prevent the Board from drawing one of them * * *." *Labor Board* v. *Nevada Copper Co.*, 316 U. S. 105, 106. The court below, while nominally deferring to these well-settled principles, in fact seriously departed from them in its review of the Board's findings in the instant case.

The operation of the presumptions.—We think, at the outset, there are two other preliminary points which should be considered. Subdivision (b) provides that the fact that a corporation is a mere holding or investment company or that its gains or profits are permitted to accumulate beyond the reasonable needs of the business "shall be prima facie evidence of a purpose to escape the

surtax." The court below thought that these presumptions[17] were of no moment since the taxpayer in any event had the burden of proof in every tax case by virtue of the presumption of correctness attaching to the Commissioner's determination and its position as petitioner in the proceedings before the Board (IV R. 1284–1285). The court made the rather inexplicable statement that "so far as the presumption is concerned, § 104 (b) would seem not to amount to much" (IV R. 1285). Under this view subdivision (b) adds nothing—a result inconsistent with the familiar rule that, if possible, significance shall be accorded every word of a statute. *Ex parte Public Bank*, 278 U. S. 101, 104; *McDonald* v. *Thompson*, 305 U. S. 263, 266; *Ginsberg & Sons* v. *Popkin*, 285 U. S. 204, 208.

To be sure, there is a presumption of correctness that attaches to the Commissioner's determination in the ordinary tax case,[18] and the taxpayer, as the moving party before the Board of Tax Appeals normally has the burden of proof. But these factors throw no light on the scope of the issues in

[17] They were so referred to by Mr. Justice Brandeis in the *National Grocery* case, 304 U. S. at p. 294, and we accordingly adopt that terminology. In the present context, however, the expression "presumption" adds very little, for the effect to be accorded presumptions varies with the reasons of policy which bring them into play. See, e. g., Morgan, *Some Observations Concerning Presumptions*, 44 Harv. L. Rev. 906, 912–914, 931–932 (1931).

[18] See *Wickwire* v. *Reinecke*, 275 U. S. 101, 105; *Welch* v. *Helvering*, 290 U. S. 111, 115; *J. M. Perry & Co.* v. *Commissioner*, 120 F. 2d 123, 124 (C. C. A. 9th); *Helvering* v. *Talbott's Estate*, 116 F. 2d 160, 162 (C. C. A. 4th).

controversy or the significance to be accorded particular evidence. It is in this connection that important effect may, and we think plainly should, be given Section 104 (b). Congress has recognized that proof of "purpose" might become difficult by reason of its subjective character; it has therefore sought to afford ease of proof of taxability by singling out two of the many subsidiary facts which may be developed in cases of this kind and requiring that very special weight should be given them. Although the ultimate point of inquiry remains whether the corporation has been formed or availed of to avoid surtaxes on its shareholders, Congress has undertaken to give guidance and direction to that inquiry and has in effect stated that the tax shall be imposed when the facts giving rise to the presumption have been established, unless the Board is satisfied that the condemned purpose was absent.

Nor is it an answer to the effectiveness of the presumptions to say, as did the court below (IV R. 1285, 1289), that they have a "logical core" apart from Section 104 (b).[18] In the absence of the presumptions it might plausibly be argued that the fact that the corporation is a mere holding or investment company or that its profits have been permitted to accumulate beyond the reasonable needs of its business in itself proves nothing, since,

[18] It is not essential, of course, that presumptions have logical bases and some, such as the presumption of survivorship among the victims of a common disaster, do not.

quite apart from tax considerations or even the existence of an income tax law, the shareholders might see no advantage in accumulating such profits in their individual bank accounts rather than in the corporation's bank accounts. By the adoption of the presumptions, Congress has foreclosed any such contention. It has in substance declared that the proper operation of the revenue laws—individual income being taxed at more steeply graduated rates than corporation income—requires the assumption that, except as reasonably needed for the operation of its business, a corporation normally pays out its earnings in dividends to its shareholders. Consequently, in the judgment of Congress, a finding that this has not been done provides a sufficient basis for the tax imposed by Section 104.

Moreover, the contrasting provisions of the two presumptions clearly indicate that in referring to "the reasonable needs of the business," in the second presumption, the statute means the reasonable needs of an active enterprise, engaged in the production of goods or the rendering of services, as distinguished from the "business" of merely holding or investing in the underlying shares of an enterprise. This is shown by the fact that the latter type of corporation is separately dealt with in the first presumption, and that, as to such corporations, the existence of *any* surplus is sufficient to erect the presumption. It is also shown by the 1924

amendment to the provision corresponding to Section 104 in the Revenue Act of 1921 and the earlier revenue acts. Section 220 of the Revenue Act of 1921, c. 136, 42 Stat. 227, had limited the first presumption to the case of "a mere holding company." Under this language the Treasury was confronted with the argument that an investment company, whose "business" it was to invest its net income, fell outside the holding company presumption, and could justify an accumulation to satisfy its investment requirements. To meet this contention, Section 220 of the Revenue Act of 1924, c. 234, 43 Stat. 253, extended the presumption to include a mere holding "or investment company." See H. Rep. No. 179, 68th Cong., 1st Sess., p. 22 (1939–1 Cum. Bull. (Part 2) 257); S. Rep. No. 398, 68th Cong., 1st Sess., p. 26 (1939–1 Cum. Bull. (Part 2) 284); Cong. Record, Vol. 65, Part 7, pp. 7354–7355.

The presumptions so established are, of course, not conclusive; the taxpayer may be able to overcome them. Even here, however, the facts underlying the presumptions narrow the type of countervailing evidence which may be considered. Proof of an investment purpose, for example, will obviously not suffice, for the existence of an investment company in itself gives rise to a presumption of the forbidden purpose. Furthermore—and here the court below did not express disagreement—by the force of Section 104 (b) the trier of fact, as indicated is authorized and indeed required to infer

from the facts underlying both or either presumption the existence of the condemned purpose unless he is persuaded by the taxpayer's further evidence that the purpose is absent. As applied to the reviewing court, the effect of the presumptions would appear to be even more decisive. When the Board or trial court has found against the taxpayer on the basis of one or both presumptions and the findings upon which the presumptions rest are supported by substantial evidence, the review is ended. It is no part of the function of the reviewing court to determine whether the presumption is displaced. *J. M. Perry & Co.* v. *Commissioner,* 120 F. 2d at p. 125; see *United Block Co.* v. *Helvering,* 123 F. 2d 704 (C. C. A. 2d), certiorari denied, 315 U. S. 812. For, to enter this field would require an appraisal and weighing of the countervailing evidence—a role not open to the appellate court.

In these circumstances, it seems patently erroneous to conclude, as did the court below, that the presumptions of Section 104 (b) add nothing to the statute. It is difficult to say to what extent such views colored its consideration of the case.[20] No doubt they had some effect, and to the extent that the court believed a mere investment program

---

[20] It is true, of course, that the presumptions are no more than tools, and that an ultimate finding of the forbidden purpose may be warranted although neither presumption is established. *United Business Corp.* v. *Commissioner,* 62 F. 2d at p. 755; *United States* v. *R. C. Tway Coal Sales Co.,* 75 F. 2d 336, 337 (C. C. A. 6th).

in an active enterprise to be inconsistent with the purposes of tax avoidance, these views may account for its disposition of the case. If uncorrected, moreover, they are calculated in other instances to work damage in the consideration given this type of case by the Board and the district courts. And errors of this kind, when intermingled with the fact-finding function, may be impossible to isolate and correct on review.

The fact that the taxpayer corporation has a single dominant shareholder.—Since a single individual, Prince, owned, for all practical purposes, the taxpayer's entire capital stock, we have here an example of that "domination and control * * * so obvious in a wholly owned corporation." *Higgins* v. *Smith*, 308 U. S. 473, 476. And see *Griffiths* v. *Commissioner*, 308 U. S. 355, 357–358. The Board's opinion accordingly referred to the taxpayer as "the *alter ego* of Prince," or as "Prince in corporate clothes" (III R. 946), as plainly was the case. The Circuit Court of Appeals expressed considerable impatience with this approach. It asserted that this "does not advance the argument much" (IV R. 1288), and insisted that (IV R. 1291–1292):

> The corporate needs must be judged from the standpoint of the corporation doing business as a legal entity separate and distinct from its shareholders. It is hardly fair to argue as the Board does: "It was of no mo-

> ment to Prince whether the earnings of the petitioner were carried in his individual pocketbook or in his corporate pocketbook, except that if they had been received in the first instance in his individual pocketbook or distributed to him by the petitioner, he would have been subjected to heavy surtaxes upon them, while he avoided such surtaxes by retaining them in the corporation." Prince is mortal; petitioner is endowed with at least potential immortality. A corporation would not be providing adequately for its own needs and legal commitments if it paid out all of its earnings in dividends and relied upon its stockholders coming to its rescue as the need arose.[21]

Apparently referring to the second presumption, the court seemed to recognize that there "is a necessary distinction * * * between the corporation's reasonable business needs and the personal ambitions of Prince, its sole stockholder," but said that this was "difficult to draw in a case like the present" (IV R. 1293).[22]

---

[21] The sentence quoted by the court is from the Board's opinion at III R. 946.

[22] Elsewhere in the opinion, however, the court seems to adopt a contrary approach, urging that the supervisory activities of Prince as an individual must be imputed to the taxpayer (IV R. 1288). We think the court overlooked the fact that while the taxpayer could act only through Prince, Prince could act other than through the taxpayer. To Prince, the taxpayer was only one of the several devices at his command. (See *infra*, pp. 50–51.)

The court below, we submit, has interwoven the unsound and the sound approach to problems of this character. Realistically, the taxpayer could have no purpose other than that which Prince imputed to it (see *United Business Corp.* v. *Commissioner*, 62 F. 2d at p. 756), and Prince's worth was increased equally whether the taxpayer added to its earned surplus or Prince added to his bank account. To blind ourselves to these facts provides no solution for this type of case, and Section 104 requires no such gingerly treatment of the corporate fiction as that indulged by the court. On the other hand, for the sake of appraising the "business needs" of a corporation under Section 104, there is a severe limitation upon the purpose which may be imputed to the corporate entity by its shareholders. Apart from the statute, an individual no doubt can impute to his corporation the declared purpose of making him a millionaire by using its earnings for the purchase of all the stock of an enterprise; but he cannot raise any such program to the dignity of a corporate purpose within the scope of Section 104.

The weight to be attributed to the fact that all the corporation's shares are held by a single individual is indicated by the principle underlying Section 104 (b) and the decision of this Court in the *National Grocery* case, *supra*. Where the corporation is engaged in an active business, entailing the production of goods or the rendering of serv-

ices, and its accumulated profits do not exceed the amount normally required for working capital, no inference of the forbidden purpose can properly be drawn from the mere existence of a surplus. While even here the sole stockholder would be no worse off if he received the income of the corporation directly and paid the expenses of the business from funds in his own hands, an inference arises from the existence of a going business that the funds which it produces are dedicated to its continuance. In the case of a business corporation whose shares are widely held, the amount of the accumulation may be sufficient even to provide for a moderate expansion of its facilities or the payment of outstanding obligations incurred for capital investment before any inference of the forbidden purpose arises; for in such a case it may be impracticable to rely upon many different stockholders individually to accumulate the funds upon which the business may wish to draw, and the fact that the shareholders are numerous diminishes the force of the contrary inference that the accumulation is made to serve the selfish purpose of a few. In this situation, otherwise expressed, there are still practical reasons for believing that the accumulations are dedicated to the requirements of the business. In the case of even a business corporation controlled by a single dominant stockholder, however, the existence of a surplus in excess of its working capital requirements

justifies an inference of the forbidden purpose. The reason here is that the funds of the corporation are at all times subject to the command of a single individual and, once the profits exceed the day to day requirements of the continuance of the business, the practical assurance that the accumulation is earmarked for business needs disappears. This consideration seems to underlie the following passage from the opinion of this Court in the *National Grocery* case, a part of the opinion which the court below appeared not to notice (304 U. S. at p. 294):

> Since Kohl was the sole owner of the corporation, the business would have been as well protected against unexpected demands for capital, and assured of capital for the purpose of any possible expansion, *by his personal ownership of the securities as by the corporation's owning them.* * * * [Italics supplied.]

A fortiori, where the corporation merely holds the stock in other companies and invests and reinvests its income, the existence of a surplus warrants an inference of the forbidden motive. For a corporation of this type exists solely and directly to increase the worth of its stockholders through the medium of enhancing its own capital worth. There is thus lacking even the assurance present in the case of a corporation actively engaged in a trade or business that its profits are dedicated to any purpose other than the immediate increase of the personal fortunes of those in control. And where the

character of such a corporation is drawn into question, the fact that all its shares are held by a single dominant stockholder would seem to be virtually decisive. Any claim that accumulation is made against "unexpected demands for capital" on the part of the companies in which stock is held or for an "expansion" of the corporation's stock holdings is answered by the fact that disbursements for such purposes could be as well made from the funds of the stockholder directly.[23]

We submit, therefore, that the fact that a single stockholder dominates the taxpayer corporation is highly pertinent to the determination both of the facts giving rise to the presumptions established by Section 104 (b) and of the ultimate fact of the existence of the condemned purpose.

I

THE BOARD'S FINDINGS AS TO THE CHARACTER OF THE TAXPAYER'S ACTIVITIES ARE SUPPORTED BY SUBSTANTIAL EVIDENCE

Rejecting the taxpayer's contention "that it supervises and directs the policies and business

[23] It should also be noted that a sole stockholder, in case of doubt, can easily protect his corporation against the tax imposed by Section 104 by the simple expedient, provided in Section 104 (d), of returning as a part of his own gross income his undistributed share of the corporation's net income. This expedient is less readily available to a group of shareholders, since Section 104 (d) provides that this action shall relieve the corporation from the Section 104 tax only where "all" of the shareholders have so returned their undistributed shares.

operations, other than the daily routine, of all the companies constituting the stockyards enterprise, and acts as banker for them" (III R. 935), the Board first found as an ultimate fact that the taxpayer is a "mere holding or investment company" (III R. 932, 935–939). In support of its determination, the Board expressly referred to the fact that in all of its income-tax returns for the years 1930–1933 the taxpayer described its business as that of "acquiring and guaranteeing securities" (III R. 937; I R. 478–479, Ex. 41–44);[24] that so far as appeared no securities were guaranteed after October 1, 1914 (III R. 937); that the payments guaranteed were amply provided for by the Jersey Company and the taxpayer had never been required to pay out a dollar on this account (III R. 937, 943–944, 913–914, 930–931; I R. 41–61, Ex. S–26; I R. 525, 526, 570–571, Ex. C, D, JJJJ–MMMM); that its income during the taxable years consisted solely of interest, dividends, and profits from the sale of securities (III R. 937, 922; I R. 478–479, Ex. 41–44); and that it used its funds principally for loans and investments in additional income-producing assets (III R. 937, 939–940; I R. 478–479, 526, Ex. 41–44, D). It also appeared, as the Board pointed out, that the taxpayer received no fees for the management or supervision of other corporations. Its office was Prince's office at 1 Court Street, Boston.

[24] The references before the semicolon are to the Board's opinion and findings; the remaining references are to the supporting evidence.

It had practically no office expenses and no rent except vault rent. Apart from Prince's salary of $50,000 it paid only salaries of $500 and "wages" of $2,000 per annum. (III R. 937, 938, 929; I R. 478–479, Ex. 41–44.) During the years 1930–1933 Prince was president of the Jersey Company and chairman of the boards of directors of the Transit Company and the Railway Company, receiving as compensation the respective amounts of $17,500, $17,500.08 and $12,499.92 for each year. The consolidated returns filed by the Jersey Company and its subsidiaries for these years represented that Prince devoted 58% of his time to the Transit Company and 42% of his time to the Railway Company for the years 1930–1932, and "part" of his time to each of the three companies for the year 1933. (III R. 938, 929; I R. 570–571, Ex. JJJJ–MMMM.) It also appeared that Prince and McDonough were trustees of the District (I R. 243). Accordingly, the Board found that the taxpayer did not in fact supervise or manage the other corporations making up the enterprise. The Board said (III R. 938):

> It is true, of course, that Prince supervised the operations of the Jersey Co. and all of its subsidiaries as well as of the subsidiaries of the petitioner. He was enabled to do this through ownership of all the stock of the petitioner, which had virtual control through stock ownership of the other corporations. He was president of the Jersey Co., from which he received an annual sal-

ary of $17,500. He was also chairman of the board of directors of the Transit Co., from which he received a like salary, and chairman of the board of directors of the Railway Co., from which he received a salary of $12,499.92. He dictated the policies of the petitioner and of all of the other companies. It does not appear, however, that the petitioner supervised and managed the operations of its subsidiaries and those of the Jersey Co. and its subsidiaries. Prince did this himself. So far as appears, there were no meetings of the board of directors of the petitioner for the determination of any acts to be done by any of the companies. The returns of the Transit Co. and the Railway Co. report Prince as devoting 58 percent of his time to the affairs of the former and 42 percent to the latter. *When directing the affairs of those companies Prince was acting as a paid employee of those companies and not of the petitioner.* [Italics supplied.]

The finding that the taxpayer was "a mere holding or investment company", raised the presumption of the condemned purpose established by Section 104 (b). And since, on the Board's appraisal, the other evidence failed to show that the taxpayer was not availed of to prevent the imposition of surtaxes on its stockholders (111 R. 939), this finding standing by itself, if valid, was sufficient to dispose of the case.

While overturning the Board's determination on this point, the Circuit Court of Appeals found no

fault with the Board's definition of a "mere holding or investment company"[25]; nor did it find that the Board had employed what the court referred to in another connection as an improper "legal yardstick" in reviewing the evidence (IV R. 1285–1288). The court simply concluded on the facts that the Board's was not a "permissible finding on the record, particularly in view of the subsidiary facts found by the Board" (IV R. 1285). In support of this conclusion the court drew its own picture of the taxpayer's operation, as follows (IV R. 1286):

> In the present case, petitioner was formed to be the directing head of the whole in-

[25] In the Board's view, the expression "mere holding or investment company" was used to differentiate a holding or investment company actively engaged in a trade or business from one whose sole income was from interest, dividends, and profit and whose sole activities were limited to those incident to an ordinary holding or investment company (III R. 935). This definition seems consonant with the purpose of the presumption and is supported by the decisions. *Wilson Bros. & Co.* v. *Commissioner*, 124 F. 2d 666 (C. C. A. 9th); *Haffer* v. *Commissioner*, 103 F. 2d 487 (C. C. A. 5th), affirming 37 B. T. A. 851, certiorari denied, 308 U. S. 576, rehearing denied, 308 U. S. 635; *Almours Securities* v. *Commissioner*, 91 F. 2d 427 (C. C. A. 5th), affirming 35 B. T. A. 61, certiorari denied, 302 U. S. 765, rehearing denied, 303 U. S. 666; *Keck Inc. Co.* v. *Commissioner*, 77 F. 2d 244 (C. C. A. 9th), affirming 29 B. T. A. 143, certiorari denied, 296 U. S. 633; *R. & L., Inc.* v. *Commissioner*, 84 F. 2d 721 (C. C. A. 5th), affirming 33 B. T. A. 857, certiorari denied, 299 U. S. 588. Moreover, special weight should be attached to the Board's judgment of a question of this character, connected as it is with the fact-finding function. Cf. *Gray* v. *Powell*, 314 U. S. 402, 411–413.

> tegrated enterprise, supplanting, in that respect, the Jersey Company, which became a "mere shell." Its purpose was to keep the enterprise intact, not to milk it dry and allow it to disintegrate in 1940. The commitments petitioner made in 1911 by guaranteeing dividends of 9 percent on the common stock of the Jersey Company, and the guarantee it made in the "by-pass agreement" of 1914, made it necessary for petitioner, in protection of its investment, to exercise an active supervision over the underlying operating companies, whose continued success was so vital to its own financial health. Since under the by-pass agreement, it drew up into its own treasury the earnings of the subsidiary companies without allowing the individual companies to make the accumulations which they normally would have needed for their own corporate purposes, petitioner, as banker for the enterprise, necessarily had to have a very substantial accumulation of funds at its disposal.

In the court's view, "the enterprise is a close-knit organism composed of many corporate members, of which petitioner is the corporate head, supplying the direction and coordination" (IV R. 1287).

If this description of the taxpayer's activities were required by the evidence, or if it followed necessarily from the Board's subsidiary findings, one might concede that the taxpayer falls short of being a mere holding or investment company.

We submit, however, that it does not follow from the evidence, that it is plainly inconsistent with the Board's findings, and that the Board's contrary determination is amply supported by substantial evidence. Manifestly, the court's view of the nature of the taxpayer's activities does not follow as a matter of law from the undisputed fact that the taxpayer is the top holding company of a vast enterprise, or that it was necessary for some man or group of men to direct the operations of the several operating companies, or that the taxpayer through its stock holdings and contractual rights was the technical repository of power over the enterprise. But it is also true that the court's determination, to the effect that the taxpayer supervised the operations of the subsidiaries and acted as banker for them, does not necessarily follow from the facts, likewise not in dispute, (1) that the taxpayer's sole stockholder, Prince, actively directed the affairs of the enterprise, or (2) that the taxpayer drew into its own treasury amounts which the underlying companies might have retained for their own requirements. Since the court seems to have based its decision of the entire case primarily upon these circumstances (IV R. 1271–1272, 1274–1276, 1286–1290, 1296–1297), we think it is advisable to consider them in detail.

(1) The Board found that it was not the taxpayer which supervised and directed the opera-

tions of its subsidiaries and those of the Jersey Company and its subsidiaries but that "Prince did this himself" (III R. 938). Criticizing this finding the court commented (IV R. 1288):

> How else could petitioner act except through the human beings who were its officers? Every corporation is controlled by some human being or group of human beings, but it is of the essence of the corporate privilege that the acts of the human beings in the exercise of the corporate powers are attributed to the corporation as a separate legal entity. It is all right to speak of petitioner as "Prince in corporate clothes"—so, if a partnership of fifteen members incorporates, the corporation may be described as the partnership in corporate clothes. This does not advance the argument much. Prince's stock ownership enabled him to sit in the driver's seat as president of petitioner. In that capacity he exercised petitioner's corporate powers. Among these powers, as the Board itself said, was petitioner's "virtual control through stock ownership of the other corporations" in the enterprise. It is of no significance in this connection that "petitioner received no fees for management and supervision"; under the circumstances, this would have been a superfluous bookkeeping formality. Nor is it important that petitioner "had practically no office expenses," and no large force of employees. For general supervision of the

> enterprise it needed only the brains of an executive of high caliber. Prince has been receiving $50,000 a year as president, and petitioner has regularly deducted this expense on its income tax returns, without challenge from the Commissioner, so far as appears.

We think that there is nothing in these observations which properly casts doubt upon the determination of the Board. Giving full play to the fiction of independent corporate personality, the taxpayer as the top holding company of the stockyards enterprise was in a position to supervise and control at every point the activities of the various subsidiaries. For this purpose the taxpayer might have built up a large staff of operating men, including a force of analysts and statisticians; it might have collected the entire gross income of all the operating units and paid the day-to-day expenses of the operations from its own funds. If this had been done, the taxpayer indeed would have been inextricably interwoven with the wealth-producing functions of the enterprise. But obviously nothing made it "necessary," as the court thought (IV R. 1286), for the taxpayer to fill this role. Its continued corporate existence under the laws of Maine did not require it to direct anyone; no contract required it; for the protection of its stock investment and its position under the guarantees of October 1, 1914, it might have been content to rely upon the selection of compe-

tent directors and officers for the underlying companies and to permit them to run these units without injecting itself into their affairs.[26] In short, it would have been no disparagement of the taxpayer's corporate personality or separate legal entity for it to have served merely as a repository for the collection of dividends or interest. Or, as a third alternative, the taxpayer might have authorized the directors and officers of the operating companies to rely upon the advice and supervision of some third agency. Invocation of the corporate fiction throws little light on what was actually done."

The course which the taxpayer did follow depended on the wishes, prior to 1922, of Prince and Arthour jointly, and, after 1922, of Prince alone. During the latter period the taxpayer was completely controlled by Prince and any fair diagram of the stockyards enterprise would either omit both the taxpayer and Prince or include both, since it was Prince, and not the taxpayer, who was the top repository of power. After 1922, therefore, the taxpayer could have no purpose or activities apart from Prince. The converse, however, was not true. Prince was free to use the taxpayer or not as he saw fit, just as he was free

[26] The evidence is uncontradicted that prior to 1926 the operating men in Chicago did manage the activities of the underlying companies "without any material control from the East" (1 R. 142–144, 290). During this period reports of operations were sent, not to the taxpayer, but to F. H. Prince & Company (1 R. 143).

to use his wholly-owned brokerage house, F. H. Prince & Company or his wholly owned Pau Corporation, in connection with the protection and expansion of his investment in the stockyards enterprise.[27] Similarly, Prince could have managed the affairs of at least some of the operating companies by reason of his being an officer in them. Or, he could act in his individual capacity without the insulation of a corporate identity or corporate office. With respect to the actual management of the units of the enterprise, the same alternatives which were open to the taxpayer were obviously open to Prince. True, orders given by Prince as an individual would carry weight only because of the recognition that ultimate power over the enterprise rested in him. But they carried precisely the same weight whether or not Prince utilized the taxpayer's corporate machinery for the purpose *or whether Prince, indeed, held any office in the taxpayer's organization.* Thus, the fact that

[27] Prince in fact did use both of these companies in this connection. For example, over many years prior to 1918 Prince purchased through F. H. Prince & Company some 18,000 shares of Jersey Company common, which he did not transfer to the taxpayer until the latter year (III R. 946–947, 927; I R. 325). As to the Pau Corporation, see *supra*, pp. 10–11. It will be noted that the diagram of the enterprise adopted by the court erroneously shows the Pau Corporation to be wholly owned by the taxpayer, rather than by F. H. Prince & Company (IV R. 1267 and annexed insert). The Board's finding, based upon a stipulation, is to the contrary (III R. 911; I R. 68; cf. I R. 323).

directions and orders were found to have been issued by Prince provided no easy solution for the problem which faced the Board.

The theory of the court—that the direction of the enterprise necessarily flowed from the holder of legal title to the stock—becomes even more artificial when viewed in the light of the obvious purpose of the holding-company presumption. The basis of the presumption is found in the fact that the mere circumstance that a company holds stock in an enterprise does not ordinarily entail the active management of a business on its part. Evidence that the holding company does run the business is inconsistent with the presumption, since it *prima facie* shows a need on the part of the holding company for the accumulation of substantial sums to meet the requirements of the business. But where, as here, the holder of the stock has not built up an organization for the management of an enterprise and the only directions given are those of its sole stockholder and his personal assistant, the reasons for removing it from the holding-company presumption are lacking.

Accordingly, there is no escaping the conclusion that it was the duty of the Board to make a careful appraisal of all the evidence which bore upon the question of whether the taxpayer actively managed the enterprise. This the Board did.

Finally, the court seized upon and quoted (IV R. 1287–1288) a long passage from the findings of the Board which, in the court's view, were inconsistent with the Board's ultimate finding on the question of management and supervision. This finding (III R. 929–930), as quoted by the court, appears as follows:

> Until his death in 1926, J. A. Spoor was president of the Transit Co. and in complete control of the Transit Co., Railway Co., and Elevated Co. He sent reports to F. H. Prince & Co. in Boston. After Spoor's death Prince became chairman of the board of directors of the Transit Co. and *representatives of the petitioner went to Chicago with increasing frequency, giving orders and directions.* [Italics the court's.] There was daily contact by telephone between the men operating the companies in Chicago and the officers of the petitioner. Prince handled the stockyards banking situation from 1930 to 1933. Ultimate choice as to officers, directors, and other personnel was dictated by Prince and he decided dividend policies. He also gave instructions as to the banks in which funds were to be deposited and his authority was necessary for unusual expenditures by the Transit Co. After the destruction of part of the stockyards by fire, the president and vice president of the petitioner went to Chicago and gave orders as to what buildings should be rebuilt and how. The yards

were not entirely restored. The restoration was paid for with insurance funds received by the Transit Co. In certain instances suggestions of the officers in Chicago were rejected by Prince. In 1933 Prince refused to permit the Transit Co. to spend enough money to build fireproof hog and sheep houses requested by the men in Chicago. Prince granted permission to rebuild the amphitheatre in which the International Live Stock Exposition was held.

Produce Terminal, the Transit Co., the District, and the Railway Co. sent to the petitioner monthly reports showing a summary of operations, which, except for the District's report, were copies of reports required by the Illinois Commerce Commission, the form of reports by the Transit Co. having been devised by its auditors. The petitioner assisted the District on many occasions in financing the construction of buildings. In 1932 it furnished between $300,000 and $400,000 for one building.

In a footnote to the above (IV R. 1287), the court also quoted the testimony of A. G. Leonard, the president of the Transit Company, as follows: "Well, the Maine Company [the taxpayer] was practically in the saddle, and I was about the hired man." [28]

As an isolated matter the statement that "representatives" of the taxpayer "went to Chicago with

[28] This testimony, given on direct examination, appears at I R. 144.

increasing frequency, giving orders and "directions" may appear inconsistent with the Board's ultimate finding. It will be noted that in the same passage, however, the Board repeatedly refers to actions taken by Prince. The above finding was based upon the testimony of the taxpayer's own witnesses, including Leonard,[29] who referred interchangeably to the taxpayer and to Prince as the source of the instructions given the operating companies (I R. 142–151, 190–194, 221–222, 226, 229–230, 243–246, 252–253, 287–290). The only two persons who could have been referred to as "representatives" of the taxpayer were Prince and his assistant, McDonough (I R. 148, 286–287, 312). In Prince's absence, McDonough stepped into his shoes (I R. 287). *During this period, however, McDonough was not an officer of, and did not even receive a salary from, the taxpayer* (I R. 287, 300). Nor could McDonough recall that any corporate action had even been taken by the taxpayer's board of directors with respect to the operations of the other companies (I R. 312–313).

It was for the Board to reconcile the testimony and to draw its own inferences, and there can be no mistake as to the ultimate inference which it

[29] It is striking to contrast the treatment accorded Leonard's testimony by the court below with the treatment of a somewhat similar situation by another Circuit Court of Appeals in sustaining a finding of fact. See *Black Diamond S. S. Corp.* v. *National Labor R. Board*, 94 F. 2d 875, 878 (C. C. A. 2d), certiorari denied, 304 U. S. 579.

drew. From the foregoing survey it seems perfectly clear that there was substantial evidence to support the Board's finding that the taxpayer did not supervise and manage the operating companies.

(2) During the period from 1922 to 1933, inclusive, the taxpayer, as the Board found (III R. 1202), drew into its own treasury from the Jersey Company and its subsidiaries amounts somewhat in excess of the net earnings of these companies. The court below seems to have been greatly impressed by this fact, but this certainly does not lead to the necessary conclusion that the taxpayer was therefore acting as the "banker" for the stockyards enterprise. This circumstance, in truth, is meaningless unless all of the concomitant facts are taken into account. Here also the Board reviewed the evidence with care, directing its inquiry to the taxpayer's precise contention that it did serve as "banker" for the enterprise. The considerations bearing upon this issue are as follows:

(A) Despite the vast sums which the taxpayer drew from the various subsidiaries, these companies were left with substantial resources to carry on their own operations. At the beginning of the taxable years, the liquid assets of Produce Terminal amounted to $499,575.93 and the liquid assets of the Jersey Company and its subsidiaries amounted to $9,594,363.94 (III R. 914; I R. 44–45, 525, Ex. C). Due primarily to the de-

mands of the banking crisis of 1930–1933 (I R. 199–207) these assets were substantially reduced during this period, but they nevertheless remained very considerable. At the end of 1933, the liquid assets of Produce Terminal amounted to $111,186.07 and the liquid assets of the Jersey Company and its subsidiaries amounted to $3,804,885.62 (I R. 525, Ex. C). At the end of the first taxable year, 1930, the earned surplus of the Jersey Company and its subsidiaries and of Produce Terminal approximated $18,250,000. At the end of 1933 such earned surplus approximated $17,750,000 (III R. 922–924; I R. 526, Ex. D). Only the Elevated Company showed a deficit in its earned surplus account, and this subsidiary was engaged in no active operation (I R. 224). The surplus for the other subsidiaries at the end of 1933 ranged from a low of $1,182,516, in the case of Produce Terminal, to a high of $5,699,978, in the case of the District. Under the bypass agreement of October 1, 1914, the Jersey Company was required to use its earnings to pay all expenses of operations and to provide for all its obligations (I R. 63, Ex. S–46). At no time, so far as the evidence discloses, did Produce Terminal, the Jersey Company or any of the subsidiaries of the latter find it necessary to call upon the taxpayer for operating expenses. When the South Side Elevated Railroad Company, the

lessee of the Elevated Company's line, went into receivership in 1932, the Jersey Company—referred to by the court below as a "mere shell" (IV R. 1286)—paid the rental without calling upon the taxpayer for assistance (I R. 224–225). During the banking crisis the Transit Company and Produce Terminal invested $3,750,000 in the securities held by the stockyards banks, and these two companies and the District subordinated bank deposits of $2,200,000 in order to assist such banks (III R. 914–915; I R. 199–207, 276–277, Ex. 18–20). Except possibly in the case of the District, these amounts were expended without any assistance from the taxpayer.

(B) The argument, apparently, is that the earnings of the Jersey Company and its subsidiaries which were drawn into the taxpayer's treasury remained dedicated to the business needs of the operating companies. The court below accepted this view (IV R. 1271–1272, 1292–1293). But the briefest consideration shows that the interests of Prince and the taxpayer, on the one side, were not identical with those of the Jersey Company and its subsidiaries. As a result of its guarantee of 9% dividends on the common stock of the Jersey Company (I R. 61–62, Ex. S–39, S–40, S–41) and the bypass agreement of October 1, 1914 (I R. 63, Ex. S–46), the taxpayer was assured of a handsome revenue from the Jersey Company during the life of these arrangements. It was to the tax-

payer's interests to see that the income continued to flow in. But the holders of the guaranteed common stock, as well as of all the preferred stock, retained full voting rights in the Jersey Company; and the guarantee arrangements gave the taxpayer no right to the assets upon a liquidation of the Jersey Company.[20] At the end of 1914 the taxpayer held less than one-fourth of the total voting stock of the Jersey Company, and even by the end of 1933, after the expenditure of more than $11,000,000 in such acquisition, it held less than a majority (I R. 67–68, Ex. S–59, S–60).

Funds which were permitted to remain in the Jersey Company's treasury were held in trust for the benefit of that company and all its shareholders. See *Pepper* v. *Litton*, 308 U. S. 295, 306–307. They were given a practical protection by the fact that as late as 1933 a majority of its voting stock was in hands other than taxpayer's. Jersey's corporate funds were not available for the use of one group of stockholders in order to

[20] With respect to the foregoing statements concerning the 1911–1914 agreements, we do not wish to be understood as expressing any opinion as to the legal effect of the complicated transactions involved and the respective rights of the parties under them. For present purposes, it is sufficient to accept the statement of taxpayer's counsel in this regard (I R. 100–101). Also see the testimony of the taxpayer's witness, Walker (I R. 503–504). Certainly the court below agreed that the taxpayer's and Prince's interests were not identical with those of the other Jersey shareholders (IV R. 1293). But see *infra*, pp. 72–74.

strengthen their position in relation to others; if any of its funds were used to buy in its own stock, the benefits of the purchase would accrue to the advantage of all the remaining stockholders; and similarly, the purchase of any of its bonds, outstanding in the aggregate amount of $14,000,000 and maturing in 1940 (I R. 52–53, 526, Ex. D), would redound to the advantage of the enterprise as a whole and all its stockholders.[21]

On the other hand, the funds which found their way into the taxpayer's treasury were subject to no such legal or practical restraints. Purchases of the stock of the Jersey Company or even of its bonds accrued, not to the advantage of the enterprise as a whole, but to the taxpayer alone. *The Jersey Company itself could not have justified accumulation of its profits for such purposes.* See *Williams Inv. Co.* v. *United States*, 3 F. Supp. 225, 232 (C. Cls.); *Trico Products Corp.* v. *Commissioner*, 46 B. T. A. 346, 378. Of course it was to the interest both of Prince and of the taxpayer, as a stockholder in the Jersey Company, to see that its obligations were paid off or refinanced in 1940 and that their retirement did not result in the dismemberment of the stockyards enterprise. In this, however, Prince and the taxpayer had only the interest which any other substantial investor

[21] The taxpayer's witness, Blough, agreed that for the protection of the creditors of the Jersey Company "the funds might better have been left down there" (I R. 472–474).

in the stock of the Jersey Company would have had. Their interest became coincidental with the interest of the Jersey Company only as their stock holdings approached 100%.

This diversity of interest between the taxpayer and the enterprise as a going concern would seem in itself enough to warrant the Board's rejection of the theory that the taxpayer was the "banker" for, or an integral part of, the stockyards enterprise. Certainly the taxpayer cannot assail the Board for viewing its "activities * * * in the light of manifest interest and purpose." *Texas & N. O. R. Co. v. Ry. Clerks*, 281 U. S. 548, 559. The Board, however, proceeded to analyze the use which the taxpayer in fact did make of its earnings.

(C) During the period 1930–1933, the taxpayer's earned surplus was increased by $8,643,373 (III R. 919; I R. 70, 526, Ex. D). It loaned $1,625,000 to the District, invested $3,573,218 in the securities of stockyards banks, which needed assistance (III R. 914–915, 927; I R. 280–282), subordinated deposits of $1,800,000 to the credits of others in stockyards banks (I R. 276–277, Ex. 17), and invested $1,500,000 in Western Associates, Inc., to enable it to hold the shares in a new bank (I R. 68–69). The loan of $1,625,000 to the District was used to retire fixed obligations and to purchase capital assets (I R. 246–248). Since the District at this time enjoyed a substan-

tial earned surplus, amounting at the end of 1933 to more than $5,500,000, the Board would seem to be justified in its comment (III R. 942) that the necessity for this loan, if any existed, is not shown. This loan, as well as the investment of $1,500,000 in Western Associates, Inc., amounted simply to substantial capital investments by the taxpayer. This was likewise true of the money invested in the stockyards banks. These outlays were, of course, on a different footing from other investments since the taxpayer stood to lose by them and they were thought to be required for the protection of the enterprise as a whole. They were the kind of investments, nevertheless, which any stockholder might, in unprecedented circumstances, feel called upon to make in order to protect his equity. They would seem to be good examples of the "unexpected demands for capital" referred to by this Court in the *National Grocery* case, *supra*, p. 294.

(D) In addition, the taxpayer increased its cash loans to Prince in the amount of $1,743,600 (III R. 916, 947; I R. 69, Ex. S–65), loaned $236,536 to the Pau. Corporation, wholly owned by Prince, without interest (III R. 927; I R. 68), spent about $425,000 for additional stock of the Jersey Company (III R. 927–928; I. R. 67–68, Ex. S–59, S–60), and spent $423,000 in purchasing its own 5% bonds, which did not mature until 1961 (III R. 927–928; I R. 68, Ex. S–62). Prince invested $1,000,000 of the sums loaned to him in order to purchase a large block of stock in Armour & Company. This

purchase, in part, enabled him to become chairman of the board of directors of that company and, according to the Board's finding, to retain its business for the Chicago stockyards (III R. 926; I R. 349–351). Aside from this aspect of the loan to Prince and the loans to the Pau Corporation, none of the transactions referred to in this paragraph had any bearing upon the welfare of the enterprise as a going concern. The Board, moreover, could not ignore the fact that all of the loans to Prince were made without strings, so that the taxpayer was unable to control Prince in the use he might make of them; nor could the Board ignore the circumstance that the Pau Corporation, while financially a part of the enterprise, was the personal property of Prince. Despite the fact that the taxpayer had immense sums of cash on hand, amounting at the end of 1933 to $7,645,235 (III R. 918; I R. 526, Ex. D), the evidence failed to disclose that the taxpayer had ever advanced funds to the Jersey Company for the retirement of its bonds—an action which would have strengthened the financial position of that company and its operating subsidiaries. And despite the discount at which these bonds sold from time to time, it did not even appear that the taxpayer itself had purchased any of the bonds of the Jersey Company or of the Elevated Company in preference to its program of stock purchases (III R. 925–926, 931).

(E) The taxpayer's loans to Prince, aggregating $4,848,000 at the end of 1933 (III R. 916; I R. 69, Ex. 8–G),[1] are especially revealing as to the purposes to which the taxpayer's funds were dedicated and hence the true character of its activities. Obviously, these loans put Prince personally into possession of funds which would otherwise have been available to him only through the declaration and payment of dividends. The Board expressly found (III R. 947) that there was "no satisfactory explanation of why the petitioner did not make a dividend distribution to Prince of the funds which he needed."[2]

Assuming that the taxpayer's accumulations of funds were dedicated to the welfare of the enterprise as a whole, the court below took the view that the loans were of little or no significance unless it were first determined that the taxpayer's accumulations were too large. The court thought

[1] This is apart from the taxpayer's loans of securities to Prince (III R. 916).

[2] In the following cases weight has been attributed to the fact that the taxpayer corporation made loans to its dominant stockholder or stockholders rather than paying dividends: *Helvering* v. *Nat. Grocery Co.*, 304 U. S. at pp. 293–294; *United Business Corp.* v. *Commissioner*, 62 F. 2d at p. 755; *J. M. Perry & Co.* v. *Commissioner*, 120 F. 2d at p. 126; *A. D. Sacrider, Inc.* v. *Commissioner*, 84 F. 2d 23, 24 (C. C. A. 5th), certiorari denied, 299 U. S. 577; *Wilson Bros. & Co.* v. *Commissioner*, 124 F. 2d 606, 609 (C. C. A. 9th); *Wilkerson Daily Corp.* v. *Commissioner*, 125 F. 2d 998, 1000 (C. C. A. 9th); *Olin Corp.* v. *Commissioner*, 128 F. 2d 185, 186–187 (C. C. A. 7th).

that since the loans "bore interest" and were amply secured by a deposit of collateral," they "did not impair petitioner's plan of accumulation." (IV R. 1295). The court also apparently thought that a system of loans to Prince was quite different from declaring out its earnings in dividends since a corporation should not rely "upon its stockholders coming to its rescue as the need arose" (IV R. 1292).

But even assuming, contrary to fact, that the taxpayer could justify large accumulations for its corporate needs, the loans to Prince might properly have impressed the Board as inconsistent with a plan of accumulation on the part of the taxpayer, and as showing that its purposes and plans were inextricably interwoven with those of Prince the individual. There is, of course, not a trace of evidence that "a prudent board of directors" (IV R. 1293) decided upon these loans after objective consideration as one step in an investment program. Moreover, the ample security referred to by the court consisted principally, as the Board found, *of the taxpayer's own common stock.* (III R. 917.) For example, the collateral so pledged by Prince had a value at December 31,

---

The provision for interest emphasizes, rather than detracts from the tax avoidance aspects of these transactions. For, the interest would be deductible from Prince's gross income; and although it would be included in the taxpayer's gross income, it would be taxed at corporate rates which would be less than the surtax rates applicable to Prince.

1933, of $8,664,199, of which $7,594,408 represented 21,520 shares of the taxpayer's common stock. (I R. 337, Ex. 24.) This meant, to the extent that its own shares were pledged with it, that the taxpayer held as security only an assignment of Prince's interest in its capital and surplus less the amount of the loans—assets which would have been available to it in the absence of any security. So far as this type of collateral was concerned, the taxpayer's resources were reduced by precisely the amount of the loans. In appraising the evidence for itself, the court below failed to mention the nature of the collateral.[35]

(F) As for its own obligations, the taxpayer was contingently obligated under the guarantee

---

[35] Generally, with respect to the character of the taxpayer's activities, it may be noted that Article 542 of Treasury Regulation 74 (Appendix, *infra*, pp. 90-91) provides that—

"* * * When one corporation owns the stock of another corporation in the same or a related line of business *and in effect operates the other corporation*, the business of the latter may be considered in substance the business of the first corporation. * * *" [Italics ours.]

but that

"* * * Investment by a corporation of its income in stock and securities of another corporation is not without anything further to be regarded as employment of the income in its business."

The Regulations thus require the determination of each case on its peculiar facts. Moreover, that portion of Article 542 which permits the business of a subsidiary to be attributed to the parent is inapplicable here, for it states that "it is ordinarily essential that the first corporation own *substantially all* of the stock of the second." Since the taxpayer owned only about one-half of the Jersey Company stock, it is plain that these provisions of the Regulations are inapplicable here.

agreements referred to (*supra*, pp. 7–8, 9–10), and was liable on its own bonds, outstanding in the amount of $3,227,000 at the end of 1929 and maturing in 1961 (III R. 918–920; I R. 526, Ex. D). So far as the 1911 guarantee of a 9% dividend on the Jersey Company common was concerned, the assenting stockholders had originally relied only upon the taxpayer's cash capital of $1,000,000 plus their lien upon the Jersey Company's distributions (I R. 61–62, Ex. S–39, S–40, S–41). So long as the Jersey Company remained able to make annual distributions in excess of 9%, the taxpayer needed no accumulations to meet these payments. And in view of the financial position and earnings of the Jersey Company (*supra*, pp. 56–58), the Board was justified in its view that the taxpayer's contingent liability under the bypass agreement had become of no practical importance (III R. 941). The bonds, outstanding in the amount of $3,227,000, had been issued, not to finance operations, but simply to acquire for the taxpayer additional blocks of Jersey Company common, and they were secured by the Jersey Company common so acquired (I R. 62, 67, Ex. S–42, S–59). The taxpayer did not attempt to justify the accumulations here involved on the basis of the liabilities referred to in this paragraph (Cf. I R. 354–370).[38]

[38] The court below seems to have suggested that the taxpayer might have been liable in tort to the stockholders and creditors of the Jersey Company in view of its course of conduct under the bypass agreement (IV R. 1291). We can hardly debate that question in this proceeding. Suffice to say that the taxpayer's "prudent board of directors" did not chart their course, so far as appears, on that assumption.

Moreover, in determining whether such obligations removed the taxpayer from the category of "mere holding or investment" companies, the Board was entitled to take the purpose for which the obligations had been incurred into account. See *Beim Co.* v. *Landy*, 113 F. 2d 897, 900 (C. C. A. 8th).

From the above it seems clear that there was ample evidence to support the Board's findings that the taxpayer was not an integral part of the stockyards operations but, rather, was the personal investment vehicle of Prince. Before the Board taxpayer's counsel declared that it "was organized with a view to some day owning this enterprise" (III R. 1004). We think that a fair statement of the character and purpose imputed to the taxpayer by Prince during the taxable period is the issue.

The Board's ultimate finding that the taxpayer was a "mere holding or investment company" had powerful support in the record. It was as much a finding of fact as the Board's determination in *Wilmington Trust Co.* v. *Commissioner*, 316 U. S. 164, that a certain transaction was not a "short sale." If the reviewing court had no authority to reject the finding in that case, there was similarly no authority to do so here. See also *supra*, pp. 29–30.

II

THE BOARD'S FINDING THAT THE TAXPAYER ACCUMULATED ITS PROFITS BEYOND THE REASONABLE NEEDS OF ITS BUSINESS IS WHOLLY VALID

In the alternative, the Board considered the taxpayer as a management company and examined its business needs viewed in that capacity. The Board found as an ultimate fact that the evidence failed to disclose "a reasonable need * * * for any further accumulation of gains and profits during any of the years 1930, 1932, and 1933," and that here also the countervailing evidence failed to overcome the presumption (III R. 945).

Since the court below held that the Board had failed to use the proper "legal yardstick" in appraising the reasonable needs of the taxpayer's business, it is of special importance to notice the precise reasoning of the Board upon this issue, as well as its findings and the supporting evidence. The Board pointed out that, even considered as a management company, the taxpayer required only $52,500 a year for the payment of salaries and wages in connection with the management of the enterprise, and that its annual income amply provided this (III R. 941). Secondly, the Board reviewed the other obligations of the taxpayer and assumed that some accumulation of profits might have been justified on this score. Pointing to the earned surplus of almost $20,000,000 at December 21, 1929, however (III R. 912; I. R.

526, Ex. D), the Board determined that there was certainly "no indication of the need for any further accumulation in the years 1930, 1932, and 1933" (III R. 941). The Board's finding with respect to the satisfaction of the obligations and commitments referred to in this paragraph was palpably correct, and the court below did not hold to the contrary.

The Board then discussed Prince's alleged plan of accumulating by 1940 some $36,500,000 of cash and liquid assets in the treasury of the taxpayer, Produce Terminal and the Jersey Company and its subsidiaries for the purpose of paying off in its entirety the outstanding bonded indebtedness of $23,963,000, of purchasing the outstanding preferred stock of the Jersey Company at a cost of about $6,500,000 and the remaining common stock at a cost of more than $1,000,000 and of setting aside $5,000,000 for working capital (III R. 942). The Board also reviewed the financial position of the entire enterprise at the end of 1929 and observed that it then had liquid assets of some $19,690,000 and total assets in excess of liabilities of some $40,000,000, not taking into account the fact that the books did not fully reflect the real value of certain of the fixed assets (III R. 943–944, 917–924; I. R. 525, 526, Ex. C, D). But in thus turning to the alleged plan of accumulation and the condition of the enterprise as a whole, it is clear that the Board did not regard such an

accumulation as within the taxpayer's reasonable business needs. For example, after reviewing the plan of accumulation the Board said (III R. 943):

> We do not think that an accumulation of surplus for the purposes above indicated was within the reasonable needs of the petitioner's business. As above indicated, the petitioner was obligated to pay off only $3,227,000 of the $23,960,000 bonds outstanding at the end of 1929. It had on hand more than twice as much cash as was necessary to redeem those bonds and they did not become due until 1961.
>
> Clearly, there was no reasonable need for the petitioner to acquire the balance of the common stock and the outstanding preferred shares of the Jersey Co. *Amounts spent in the acquisition of those shares simply represented investments by the petitioner.* The same also is true of any amounts that it might expend in acquiring the bonds of the Jersey Co. and its subsidiaries. [Italics supplied.]

Similarly, the Board observed that under his program Prince, through the instrumentality of the taxpayer, would own in 1940 assets of a value of more than $60,000,000, free of debt—an ambition irrelevant to the reasonable business needs of a corporation (III R. 944–945).

Even assuming, contrary to the Board's finding discussed in Point I, that the taxpayer was a management company and furthermore that its

reasonable needs might include the needs of the entire stockyards enterprise, there can still be no basis for the court's conclusion (IV R. 1292–1293) that the taxpayer's acquisition of the entire enterprise in 1940 was within the reasonable needs of the business of the enterprise. The court's theory proceeds upon the wholly false assumption that the Jersey Company would have to be "liquidated" in 1940, and that it would therefore be to the best interests of the enterprise for the taxpayer to buy out the "minority" (IV R. 1293) security holders. But there is nothing to show that such "liquidation" was inevitable, even if Jersey's charter did expire in 1940. The ease with which corporate charters may be obtained is well within the realm of judicial notice. Plainly, Jersey could have been reincorporated in 1940 without any disturbance of the continuity of the enterprise. Taxpayer's acquisition of the so-called minority interest in Jersey and the subsequent liquidation of Jersey would certainly promote Prince's ambition to own the stockyards unhampered by "minority" groups; but that objective could hardly be said to be within the reasonable needs of the stockyards enterprise. Indeed, the minority stockholders of Jersey might view the situation in quite a different light.[37]

The evidence certainly did not require a finding that the day-to-day operations of the stock-

[37] It is to be borne in mind that as late as December 31, 1933, the taxpayer owned less than a majority of the voting stock of the Jersey Company (*supra*, p. 59).

yards and the other operating units would be handicapped by the fact that a part of their stock was held by other interests; and the great success of the enterprise during the past 25 years, when the stock was so held, provides affirmative evidence to the contrary. Thus, if, as the court believed, the taxpayer had need for buying up or redeeming the shares of the Jersey Company held by others than itself, this need stemmed only from the fact that the taxpayer's interests were essentially different from the needs of the enterprise as a service-rendering and wealth-producing organization.

Similarly, the liquidation of the Jersey Company was a reasonable business need of the taxpayer, on any view, only upon the assumption that the taxpayer was to take over the entire stockyards enterprise. The testimony of the Government's expert witnesses, referred to by the court (IV R. 1291, fn. 10), was framed upon this hypothesis (II R. 660–706, 775–809, 839–848, 851–853). But here, also, the evidence certainly did not require a finding that the operating interests of the enterprise demanded the Jersey Company's liquidation. If from the standpoint of the enterprise one of the holding companies should have been eliminated, the axe might as well have fallen upon the taxpayer as upon the Jersey Company. A need for the liquidation of the Jersey Company can be imputed to the taxpayer only by attributing to it an interest and purpose separate and

apart from that of the enterprise as a going business. That the Jersey Company and its subsidiaries had no business need for the ownership of all of its shares by a single stockholder, whether the taxpayer or some other interest, seems too clear for further argument. See *Williams Inv. Co.* v. *United States*, 3 F. Supp. at 232.

In concluding that the Board had used "an improper 'legal yardstick' by which to measure" the taxpayer's needs (IV R. 1290), the court did not take the further step of holding that the accumulations of the enterprise as of December 31, 1929, were insufficient even to meet the expanded business needs which it vaguely (IV R. 1293–1295) outlined. But since the Board had failed to consider the preexisting accumulations in the light of what the court considered to be the taxpayer's true business needs, it remanded the case to the Board for findings on this point and for a reexamination of its ultimate determination in the light of such findings [38] (IV R. 1290–1291, 1296–1297).

[38] It should be observed that the remand did not leave it open to the Board to determine whether the projected 1940 "liquidation" of Jersey was within the reasonable needs of the business. The court apparently determined that question for itself. It merely left it to the Board to find whether the accumulations in question were necessary for that purpose. This was a false issue, for the court erred in finding that such a purpose was within the reasonable needs either of the taxpayer or of the enterprise as a whole.

We do not disagree, for present purposes, with the ruling of the court that (IV R. 1291)—

> Accumulation "for the reasonable needs of the business" is not limited to making provision for the bare legal obligations of the corporation but may include accumulation in furtherance of a *reasonable business program* for protection and enhancement of the corporation's pecuniary interests. [Italics supplied.][39]

But there is nothing in the Board's decision which is to the contrary. That proposition is irrelevant unless it is first determined that the taxpayer's business is that of actively operating and financing the enterprise as a whole (shown to be otherwise in Point I), and that the objective sought to be attained by the accumulation is within the reasonable needs of the enterprise (shown to be otherwise here in Point II).

Accordingly, while the court's treatment of this issue is expressed in terms of an error in law, the Board's alleged error differs essentially from that of a trier of fact which has excluded or otherwise failed to consider relevant and competent materials. Whatever the validity of the court's legal postulate as to business needs, the Board committed no error of law unless its basic

[39] As we have seen (*supra*, pp. 39–40), the court's proposition probably goes too far as applied to a one-man corporation, even when the corporation is actively operating a business. Cf. *Helvering* v. *Nat. Grocery Co.*, 304 U. S. at p. 294.

finding as to the character of the taxpayer's activity is overturned and, in addition, the well-being of the enterprise is shown to require the ownership of all its shares by a single stockholder, the taxpayer. Prince's ambition to buy out the "minority" interests and take over the entire enterprise could not, on any view, raise itself to the level of a business need of the taxpayer. The critical error of the court below lies in its failure to accord the Board's factual determination the weight to which it is entitled under the controlling decisions. If the court erred in this, it remanded the case on a false issue.

III

EVEN APART FROM THE PRESUMPTIONS, THE BOARD'S DETERMINATION IS VALID

Finally, the Board, as did this Court in the *National Grocery* case, 304 U. S. at p. 294, considered the evidence without the aid of the statutory presumptions and found that the taxpayer was "availed of" for the prohibited purpose. The Board unequivocally stated (III R. 947):

> Even without the benefit of the statutory presumptions, we think there is sufficient evidence in the record to show the existence of the condemned purpose. The bare recital of the undisputed facts relating to the organization of the petitioner, the balance sheets, the source of earnings, the nature of the investments, the large accumulations of

> cash and surplus, the loans of cash and securities to the petitioner's sole stockholder, and the continued reinvestment of its gains and profits in securities, present, in our opinion, a situation typical of situations which Congress intended to cover by section 104 of the Revenue Acts of 1928 and 1932.

The Board's opinion then makes further reference to the considerations which led to its ultimate determination. Fundamental here is a picture of the taxpayer corporation utilized by Prince as his personal vehicle for the accumulation of a vast fortune through the medium of applying the earnings of the enterprise to buy out the other security holders. To the Board the taxpayer "was the *alter ego* of Prince. It was Prince in corporate clothes." (III R. 946.) Citing the *National Grocery* case the Board concluded that (III R. 946)—

> It was of no moment to Prince whether the earnings of the petitioner were carried in his individual pocketbook or in his corporate pocketbook, except that if they had been received in the first instance in his individual pocketbook or distributed to him by the petitioner he would have been subjected to heavy surtaxes upon them, while he avoided such surtaxes by retaining them in the corporation.

The taxpayer was the means by which Prince had succeeded in accumulating up to 1929 a for-

tune of from $15,000,000 to $20,000,000 practically immune from taxation, since the taxpayer's income consisted almost exclusively of dividends from domestic corporations which were a legal deduction in determining its taxable net income (III R. 946).[*] The Board also referred to its finding that during the taxable years Prince had saved more than $1,300,000 in surtaxes by virtue of the taxpayer's failure to pay out its earnings in dividends (III R. 948, 931; II R. 853–854, Ex. YYYY). The large loans to Prince over a period of many years were again referred to (III R. 947).[**] Finally, the Board adverted to the fact

---

[*] The taxpayer's net earnings for the years 1911–1923, inclusive, aggregated $34,619,278.70 (III R. 918; I R. 63–64, 70, Ex. S-51). The evidence showed that for the years 1917 to 1933, inclusive, Prince paid individual income and surtaxes as follows (I R. 562–565, Ex. CCC–TTT):

1917	$2,242.40	1926	$5,613.56
1918	1,883.30	1927	7,060.42
1919	None	1928	46,652.80
1920	None	1929	15,656.01
1921	None	1930	51,570.96
1922	None	1931	26,061.08
1923	$197.25	1932	20,023.94
1924	1,575.77	1933	19,164.29
1925	None		

Compare the similar table appended to the opinion of this Court in the *National Grocery* case (304 U. S. at pp. 292–293, footnote 9).

[**] We have pointed out (*supra*, pp. 64–66) the error of the court below in thinking that these loans did not interfere with the taxpayer's alleged plan of accumulation, and that they lacked probative force unless it was first decided that the taxpayer's accumulations were unreasonably large.

that Prince on several occasions had effected individual tax losses by the device of selling securities to the taxpayer, and that the taxpayer had likewise taken tax losses by selling securities to F. H. Prince & Company, Inc. (III R. 947–948, 928–929, 1202; I. R. 70, 533–534, Ex. E.) The Board observed that the (III R. 948)—

> * * * shifting of these securities from Prince to the petitioner and from the petitioner to Prince really meant no economic loss to Prince and the investment by the corporation of the amounts of money spent in acquiring the securities from Prince was not in furtherance of the program which Prince claims to have had for the corporation.

We have considered a number of the above facts in connection with the character of the taxpayer's activities (*supra*, pp. 41–69), since they relate to that issue. Others, however—namely, the loans to Prince, the tax loss sales and the vast amounts of surtaxes actually avoided—have probative value apart from the character of the taxpayer's activities or its reasonable business needs. The Circuit Court of Appeals went to the verge of understatement when it said, referring to the tax loss sales (IV R. 1296): "At most, these transactions might be taken to indicate that Prince was not wholly unmindful of tax consequences nor averse on

principle to minimizing taxes." [42] Moreover, while, as the court below pointed out (IV R. 1279), it is important under Section 104 not to confuse effect with purpose, the fact of large surtax savings by Prince was undoubtedly entitled to some weight. See *Helvering* v. *Nat. Grocery Co.*, 304 U. S. at p. 292.[43] It strains credulity to believe that Prince, perhaps not "averse on principle to minimizing taxes," would have failed to recognize that adherence to his plan of accumulation could more readily be achieved by accumulating the taxpayer's earnings free of taxes than by paying an individual surtax upon them.

Once the taxpayer is viewed in its true light, as the medium through which Prince used the earnings of the operating companies to buy up the

---

[42] There is nothing to indicate that the Board regarded the tax loss sales *per se* as instances of the use of the taxpayer to avoid surtaxes "through the medium of permitting its gains or profits to accumulate" within the meaning of Section 104 (III R. 946-948). Cf. *W. S. Farish & Co.* v. *Commissioner*, 38 B. T. A. 150, 155; affirmed, 104 F. 2d 833 (C. C. A. 5th).

[43] We submit that the Board of Tax Appeals correctly appraised the weight to be given such evidence when it said in the *Blaffer* case, 37 B. T. A. at p. 856:

"* * * In the absence of the condemned purpose, the effect alone is no foundation for the tax. This is not to say that the effect is of no significance, for it may, and perhaps often does, indicate the probability of a purpose to induce it. In ordinary life it is not unreasonable to infer that the effect of a voluntary act is among the purposes of the actor. So long as the inference be not arbitrary and evidence to the contrary be entertained and fairly weighed, it may be regarded as reasonable. * * *"

underlying shares of the enterprise, it becomes perfectly clear that no purpose peculiar to the taxpayer was served by having new purchases effected in its name rather than in the name of Prince individually. In these circumstances, any scheme of investment which partly dispensed with the payment of dividends necessarily carried with it a program of using amounts otherwise payable in surtaxes for the making of additional investments. See *Williams Inv. Co.* v. *United States*, 3 F. Supp. at p. 232. In judging the weight to be given denials of the condemned purpose, it was for the Board to take all the factors into account.

While expressing dissatisfaction, as we have indicated, with certain of the Board's subsidiary findings under this third point, the court below did not hold that the Board's ultimate finding of forbidden purpose, reached without the aid of the presumptions, lacked the support of substantial evidence. It was of the view, however, that the Board's ultimate finding here was predicated "chiefly" upon its findings that the taxpayer "was a mere holding or investment company" and that it "had accumulated its profits beyond the reasonable needs of the business, coupled with the fact that Prince saved a large amount of surtaxes by the withholding of further dividends." (IV R. 1295).

But the Board's finding, explicitly stated to have been reached without the aid of the presumptions, may not be so lightly cast aside. The taxpayer's huge accumulation of its earnings, Prince's use of these funds through the device of loans rather than dividends, his use of the taxpayer to effect paper transactions for tax loss purposes, the large amount of surtaxes which he saved—all afforded powerful support for the Board's finding of the condemned purpose. They were strongly persuasive, whatever the type of corporation involved, and whatever its reasonable business needs, objectively considered. Apart from the presumptions, they are sufficient to sustain the Board's determination, since they bear directly upon the reason for the accumulation.

While misconstruing the relation of the presumptions to the Board's determination reached without the aid of them, the court below would doubtless have affirmed the Board's decision had it agreed with the Board as to the nature of the taxpayer's activities. This is shown by the fact that, after a full review of the evidence, the court's disagreement with the Board derives from the substitution of its own appraisal of the evidence for that of the Board's on this issue (IV R. 1286–1287, 1290–1291, 1295). Accordingly, there is no occasion for the remanding of the case to the Circuit Court of Appeals for further consideration. Compare *Helvering* v. *Nat. Grocery*

Co., 304 U. S. at p. 295 with *Helvering* v. *Rankin*, 295 U. S. at pp. 133–134. The decision of the Circuit Court of Appeals should be reversed and that of the Board of Tax Appeals should be affirmed.

CONCLUSION

The Board's decision rested upon three independent grounds, and the court below erred in reversing the Board on each of those grounds.

(1) After reviewing the taxpayer's activities in great detail the Board found that it was a "mere holding or investment company" within the meaning of Section 104 (b). The court below rejected that determination, stating, "We do not think that this is a permissible finding on the record * * *" (IV R. 1285). On this aspect of the case, therefore, the court's ruling was based *solely* upon a disagreement with the Board as to a finding of fact which was supported by substantial evidence. And that finding was sufficient to dispose of the entire case; for it called into play the presumption established by Section 104 (b) which, the Board found, had not been rebutted. Accordingly, if this Court should conclude that the court below erred in rejecting the Board's finding that the taxpayer was a "mere holding or investment company," the court's decision must be reversed, and that of the Board affirmed.

(2) The Board also rested its decision on a second and wholly independent ground. It found

that the taxpayer "permitted its gains and profits to accumulate beyond the reasonable needs of its business" within the meaning of Section 104 (b); and that the presumption arising from that finding had not been rebutted. On this aspect of the case the Board assumed *arguendo* that the taxpayer was more than a mere holding or investment company. It found that, even considering the taxpayer as a management company, the accumulations were beyond the reasonable needs of its business. Moreover, even assuming that the taxpayer's business needs are those of the enterprise as a whole, the accumulation of earnings for the purpose of liquidating the Jersey Company and of transferring to the taxpayer ownership of the entire enterprise does not come within the scope of such needs. So far as the enterprise was concerned, it was of no moment whether the Jersey Company was liquidated or its stock was held by few or many. Prince's ambition to liquidate the Jersey Company and own the whole enterprise could not be transmuted into a business need either of the taxpayer or the enterprise. Holding that the Board had used a wrong "legal yardstick" in measuring the taxpayer's needs, the court ordered a remand so that the Board might determine whether the accumulations were necessary for the projected liquidation of the Jersey Company. This was a false issue, for the Board

had already correctly determined that the liquidation of the Jersey Company was not within the reasonable needs of the business.

(3) The Board finally found as a fact that, irrespective of either of the two foregoing findings which gave rise to the presumptions, the earnings of the taxpayer had been accumulated for the forbidden purpose. In refusing to accept that finding the court below stated that the Board's determination "was predicated chiefly" upon the two foregoing findings, which the court had already rejected (IV R. 1295). But the court seriously erred in this respect; for the Board unambiguously stated (III R. 945): "Even without the benefit of the statutory presumptions, we think there is sufficient evidence in the record to show the existence of the condemned purpose." Accordingly, unless the veracity of this statement is to be challenged, the Board's decision must be viewed as resting independently upon this third alternative ground, which has powerful support in the record.

The court below erred in reversing the Board on each of the three grounds summarized above. Each of those grounds was sufficient, standing alone, to support the deficiency found by the Board. Accordingly, if this Court should agree that the court below erred on any one of those three grounds, the decision below must be reversed

with instructions to affirm the judgment of the Board.

Respectfully submitted.

CHARLES FAHY,
Solicitor General.

SAMUEL O. CLARK, JR.,
Assistant Attorney General.

CARLTON FOX
SEWALL KEY,
ARNOLD RAUM,
ALVIN J. ROCKWELL,
Special Assistants to the Attorney General.

FEBRUARY 1943.

APPENDIX

Revenue Act of 1928, c. 852, 45 Stat. 791:

SEC. 104. ACCUMULATION OF SURPLUS TO EVADE SURTAXES.

(a) If any corporation, however created or organized, is formed or availed of for the purpose of preventing the imposition of the surtax upon its shareholders through the medium of permitting its gains and profits to accumulate instead of being divided or distributed, there shall be levied, collected, and paid for each taxable year upon the net income of such corporation a tax equal to 50 per centum of the amount thereof, which shall be in addition to the tax imposed by section 13 and shall be computed, collected, and paid upon the same basis and in the same manner and subject to the same provisions of law, including penalties, as that tax.

(b) The fact that any corporation is a mere holding or investment company, or that the gains or profits are permitted to accumulate beyond the reasonable needs of the business, shall be prima facie evidence of a purpose to escape the surtax.

(c) As used in this section the term "net income" means the net income as defined in section 21, increased by the sum of the amount of the dividend deduction allowed under section 23 (p) and the amount of the interest on obligations of the United States issued after September 1, 1917, which would

be subject to tax in whole or in part in the hands of an individual owner.

(d) The tax imposed by this section shall not apply if all the shareholders of the corporation include (at the time of filing their returns) in their gross income their entire distributive shares, whether distributed or not, of the net income of the corporation for such year. Any amount so included in the gross income of a shareholder shall be treated as a dividend received. Any subsequent distribution made by the corporation out of the earnings or profits for such taxable year shall, if distributed to any shareholder who has so included in his gross income his distributive share, be exempt from tax in the amount of the share so included.

The provisions of Section 104 of the Revenue Act of 1932, c. 209, 47 Stat. 169, are identical with those of Section 104 of the Revenue Act of 1928, except as subdivision (a) of Section 104 of the Revenue Act of 1932 was amended by Section 214 of the National Industrial Recovery Act, c. 90, 48 Stat. 195, which provides as follows:

SEC. 214. Section 104 of the Revenue Act of 1932 is amended by striking out the words "the surtax" wherever occurring in such section and inserting in lieu thereof "any internal-revenue tax." The heading of such section is amended by striking out "surtaxes" and inserting in lieu thereof "internal-revenue taxes." Section 13 (c) of such Act is amended by striking out "surtax" and inserting in lieu thereof "internal-revenue tax."

Treasury Regulations 74, promulgated under the Revenue Act of 1928:

ART. 541. *Taxation of corporation utilized for evasion of surtax.*—Section 104 is designed to discourage the formation or use of a corporation for the purpose of preventing the imposition of surtaxes upon its shareholders, through the device of permitting its gains and profits to accumulate instead of being distributed. If a domestic or foreign corporation is so formed or availed of, it is subject to a tax at the rate of 50 percent upon its net income in addition to the tax imposed by section 13. However, the additional tax at the rate of 50 percent does not apply for 1928 or any subsequent taxable year if all the shareholders of the corporation include (at the time of filing their returns) in their gross income their entire distributive share, whether distributed or not, of the net income of the corporation for such year or years. Any amount so included in the gross income of a shareholder shall be treated as a dividend received, and any subsequent distribution made by the corporation out of the earnings or profits for such taxable years shall, if distributed to any shareholder who has so included in his gross income his distributive share, be exempt from tax in the amount of the share so included.

ART. 542 (As amended by T. D. 4470, XIII-2 Cum. Bull. 151 (1934)). *Purpose to escape surtax.*—Prima facie evidence of a purpose to escape the surtax exists where a corporation is a mere investment company, where a corporation has practically no business except holding stocks, securities, or other property and collecting the income therefrom or investing therein, or where a corporation other than a mere hold-

ing or investment company permits its gains and profits to accumulate beyond the reasonable needs of the business. The statutory presumption that a mere holding or investment company is subject to the additional tax imposed by section 104 will be overcome if the corporation can show by a disclosure of all the facts that it was not formed or availed of for the purpose of avoiding the surtax, but the mere fact that it distributed a large portion of its earnings for the year in question is not sufficient to overcome the presumption.

The business of a corporation is not merely that which it has previously carried on, but includes in general any line of business which it may legitimately undertake. However, a radical change of business when a considerable surplus has been accumulated may afford evidence of a purpose to escape the surtax. When one corporation owns the stock of another corporation in the same or a related line of business and in effect operates the other corporation, the business of the latter may be considered in substance the business of the first corporation. Gains and profits of the first corporation put into the second through the purchase of stock or otherwise may therefore, if a subsidiary relationship is established, constitute employment of the income in its own business. To establish that the business of one corporation can be regarded as including the business of another it is ordinarily essential that the first corporation own substantially all of the stock of the second. Investment by a corporation of its income in stock and securities of another corporation is not without anything

further to be regarded as employment of the income in its business.

ART. 543 (As amended by T. D. 4470, *supra*). *Unreasonable accumulation of profits.*—An accumulation of gains and profits (including the undistributed earnings or profits of prior years) is unreasonable if it is not required for the purposes of the business, considering all the circumstances of the case. It is not intended, however, to prevent reasonable accumulations of surplus for the needs of the business. No attempt can be made to enumerate all the ways in which gains and profits of a corporation may be accumulated for the reasonable needs of the business. Distributions made by a corporation shortly after the close of its taxable year shall be taken into consideration in determining the reasonableness of the amount of earnings and profits accumulated by the corporation. Undistributed income is properly accumulated if invested in increased inventories or additions to plant reasonably needed by the business. It is properly accumulated if retained for working capital required by the business or in accordance with contract obligations placed to the credit of a sinking fund for the purpose of retiring bonds issued by the corporation. In the case of a banking institution the business of which is to receive and loan money, using capital, surplus, and deposits for that purpose, undistributed income actually represented by loans or reasonably retained for future loans is not accumulated beyond the reasonable needs of the business. The nature of the investment of gains and profits is immaterial if they are not in fact needed in the business. It is the unreasonable ac-

cumulation of gains and profits by a corporation which constitutes prima facie evidence of the purpose to enable its shareholders to escape the surtax. Among other things, the financial condition of the corporation and the manner in which it[s] funds are invested determine the reasonableness of the accumulations.

For the purpose of section 104 the term "net income" means the net income of the corporation as defined in section 21 increased by the sum of (1) the amount received as dividends and allowed as a deduction by section 23 (p), plus (2) the amount of interest on obligations of the United States issued after September 1, 1917, which would be subject to tax in whole or in part in the hands of an individual owner. The Commissioner, or any collector upon direction from the Commissioner, may require any corporation to furnish a statement of its accumulated gains and profits, the name and address of, and number of shares held by, each of its shareholders, and the amounts that would be payable to each, if the income of the corporation were distributed. (See section 149 (c).)

The like numbered articles of Treasury Regulations 77, promulgated under the Revenue Act of 1932, as amended by T. D. 4470, *supra,* are substantially identical with the foregoing.

U. S. GOVERNMENT PRINTING OFFICE: 1936